EQUINIX INC
Form 10-Q
November 01, 2006
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended September 30, 2006

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from ______ to ______

Commission File Number 000-31293

EQUINIX, INC.

(Exact name of registrant as specified in its charter)

Delaware	**77-0487526**
(State of incorporation)	**(I.R.S. Employer Identification No.)**

301 Velocity Way, Fifth Floor, Foster City, California 94404

(Address of principal executive offices, including ZIP code)

(650) 513-7000

(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) Yes x No ¨ and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x	Accelerated filer ¨	Non-accelerated filer ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

The number of shares outstanding of the registrant s Common Stock as of September 30, 2006 was 29,176,241.

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PART I - FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

EQUINIX, INC.

Condensed Consolidated Balance Sheets

(in thousands)

	September 30, 2006	December 31, 2005
	(unaudited)	
Assets		
Current assets:		
Cash and cash equivalents	$ 84,639	$ 119,267
Short-term investments	61,322	52,105
Accounts receivable, net	24,129	17,237
Prepaids and other current assets	5,990	3,103
Total current assets	176,080	191,712
Long-term investments	20,385	17,483
Property and equipment, net	499,917	438,790
Goodwill	22,710	21,654
Debt issuance costs, net	2,685	3,075
Other assets	8,843	8,283
Total assets	$ 730,620	$ 680,997
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable and accrued expenses	$ 23,007	$ 22,557
Accrued property and equipment	18,597	15,783
Borrowings from credit line	40,000	30,000
Current portion of accrued restructuring charges	13,848	12,400
Current portion of capital lease and other financing obligations	1,855	1,552
Current portion of mortgage payable	1,337	1,159
Other current liabilities	8,517	7,972
Total current liabilities	107,161	91,423
Accrued restructuring charges, less current portion	30,698	37,431
Capital lease and other financing obligations, less current portion	93,220	94,653
Mortgage payable, less current portion	57,828	58,841
Convertible subordinated debentures	86,250	86,250
Deferred rent and other liabilities	27,879	23,726
Total liabilities	403,036	392,324
Stockholders equity:		
Common stock	29	27
Additional paid-in capital	887,319	839,497
Deferred stock-based compensation		(4,930)
Accumulated other comprehensive income	2,791	1,126
Accumulated deficit	(562,555)	(547,047)

Total stockholders equity	327,584	288,673
Total liabilities and stockholders equity	$ 730,620	$ 680,997

See accompanying notes to condensed consolidated financial statements

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EQUINIX, INC.

Condensed Consolidated Statements of Operations

(in thousands, except per share data)

	Three months ended September 30, 2006	Three months ended September 30, 2005	Nine months ended September 30, 2006	Nine months ended September 30, 2005
	(unaudited)			
Revenues	$ 73,726	$ 58,096	$ 207,143	$ 159,259
Costs and operating expenses:				
Cost of revenues	49,137	40,955	138,045	116,639
Sales and marketing	7,502	4,829	23,180	14,793
General and administrative	18,631	12,078	53,486	33,594
Restructuring charges	1,527		1,527	
Total costs and operating expenses	76,797	57,862	216,238	165,026
(Loss) income from operations	(3,071)	234	(9,095)	(5,767)
Interest income	1,724	1,075	5,065	2,644
Interest expense	(3,551)	(1,928)	(10,984)	(6,332)
Loss before income taxes and cumulative effect of a change in accounting principle	(4,898)	(619)	(15,014)	(9,455)
Income taxes	(270)	(164)	(870)	(553)
Net loss before cumulative effect of a change in accounting principle	(5,168)	(783)	(15,884)	(10,008)
Cumulative effect of a change in accounting principle for stock-based compensation (net of income taxes of $0)			376	
Net loss	$ (5,168)	$ (783)	$ (15,508)	$ (10,008)
Net loss per share:				
Basic and diluted net loss per share before cumulative effect of a change in accounting principle	$ (0.18)	$ (0.03)	$ (0.56)	$ (0.43)
Cumulative effect of a change in accounting principle			0.01	
Basic and diluted net loss per share	$ (0.18)	$ (0.03)	$ (0.55)	$ (0.43)
Weighted-average shares	28,743	24,076	28,356	23,335

See accompanying notes to condensed consolidated financial statements

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EQUINIX, INC.

Condensed Consolidated Statements of Cash Flows

(in thousands)

	Nine months ended September 30, 2006	2005
	(unaudited)	
Cash flows from operating activities:		
Net loss	$ (15,508)	$ (10,008)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation	52,200	46,504
Stock-based compensation	23,540	6,291
Accretion of asset retirement obligation and accrued restructuring charges	2,795	1,043
Amortization of intangible assets and non-cash prepaid rent	833	240
Non-cash interest expense	643	1,451
Allowance for (recovery of) doubtful accounts	16	(457)
Loss on disposal of assets	6	4
Cumulative effect of a change in accounting principle	(376)	
Restructuring charges	1,527	
Changes in operating assets and liabilities:		
Accounts receivable	(6,908)	(3,823)
Prepaids and other assets	(2,305)	647
Accounts payable and accrued expenses	470	3,602
Accrued restructuring charges	(9,213)	(1,448)
Other liabilities	1,833	4,990
Net cash provided by operating activities	49,553	49,036
Cash flows from investing activities:		
Purchases of investments	(68,619)	(100,693)
Sale of investments		13,360
Maturities of investments	56,789	103,344
Purchase of Chicago IBX property	(9,766)	
Purchases of other property and equipment	(102,904)	(57,219)
Accrued property and equipment	2,814	2,245
Proceeds from sale of property and equipment	8	
Net cash used in investing activities	(121,678)	(38,963)
Cash flows from financing activities:		
Proceeds from exercise of warrants, stock options and employee stock purchase plans	28,756	11,217
Proceeds from borrowings under credit line	40,000	
Repayment of borrowings from credit line	(30,000)	
Repayment of capital lease and other financing obligations	(1,130)	(4,213)
Repayment of mortgage payable	(835)	
Debt issuance costs	(253)	(342)
Excess tax benefits from stock-based compensation	814	
Net cash provided by financing activities	37,352	6,662

Effect of foreign currency exchange rates on cash and cash equivalents		145		(100)
Net increase (decrease) in cash and cash equivalents		(34,628)		16,635
Cash and cash equivalents at beginning of period		119,267		25,938
Cash and cash equivalents at end of period	$	84,639	$	42,573
Supplemental cash flow information:				
Cash paid for taxes	$	545	$	
Cash paid for interest	$	11,352	$	5,277

See accompanying notes to condensed consolidated financial statements

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EQUINIX, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation and Significant Accounting Policies

The accompanying unaudited condensed consolidated financial statements have been prepared by Equinix, Inc. (Equinix or the Company) and reflect all adjustments, consisting only of normal recurring adjustments, which in the opinion of management are necessary to fairly state the financial position and the results of operations for the interim periods presented. The balance sheet at December 31, 2005 has been derived from audited financial statements at that date. The financial statements have been prepared in accordance with the regulations of the Securities and Exchange Commission (SEC), but omit certain information and footnote disclosure necessary to present the statements in accordance with generally accepted accounting principles. For further information, refer to the Consolidated Financial Statements and Notes thereto included in Equinix s Form 10-K as filed with the SEC on March 16, 2006. Results for the interim periods are not necessarily indicative of results for the entire fiscal year.

The preparation of consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

The Company believes it has sufficient cash, coupled with anticipated cash generated from operating activities and anticipated cash from financings expected to close in the fourth quarter of 2006 as described below, to meet its currently identified business objectives for at least the next twelve months. As of September 30, 2006, the Company had $166,346,000 of cash, cash equivalents and short-term and long-term investments. Since the quarter ended September 30, 2003, the Company has generated positive operating cash flow in each quarter and expects this trend to continue throughout the remainder of 2006 and beyond. In addition, as of September 30, 2006, the Company had $28,300,000 of additional liquidity available to it under the Company s Silicon Valley Bank Credit Line Amendment, which was amended in August 2006 (see Note 9), in the event the Company needs additional cash to fund expansion activities, fund working capital requirements or pursue attractive strategic opportunities that may become available in the future. In September 2006, the Company received loan commitments, subject to customary closing conditions, for a total of $150,000,000 to finance its Washington, D.C. Metro Area IBX Expansion Project (see Note 2) and Chicago Metro Area IBX Expansion Project (see Note 2) in long-term financing arrangements at anticipated rates of approximately 8%, which the Company expects to close during the fourth quarter of 2006. While the Company expects that its cash flow from operations will continue to increase, the Company expects its cash flow used in investing activities, primarily as a result of its expected purchases of property and equipment to complete these expansion projects, will also increase (see Note 12, Other Purchase Commitments) and the Company expects them to be greater than its cash flows generated from operating activities. As a result, while the Company believes it has sufficient cash, coupled with anticipated cash generated from operating activities and anticipated cash from financings expected to close in the fourth quarter of 2006, to meet its currently identified business objectives for at least the next twelve months, the Company will investigate additional financing opportunities in connection with the Company s current and future expansion plans, in order to continue to meet its cash requirements to fund its other capital expenditures, debt service and corporate operating requirements and maintain its cash and working capital position.

Revenue Recognition and Allowance for Doubtful Accounts

Equinix derives more than 90% of its revenues from recurring revenue streams, consisting primarily of (1) colocation services, such as from the licensing of cabinet space and power; (2) interconnection services, such as cross connects and Equinix Exchange ports; (3) managed infrastructure services, such as Equinix Direct, bandwidth, mail service and managed platform solutions and (4) other services consisting of rent from non-IBX space. The remainder of the Company s revenues are from non-recurring revenue streams, such as from the recognized portion of deferred installation revenues, professional services, contract settlements and equipment sales. Revenues from recurring revenue streams are billed monthly and recognized ratably over the term of the contract, generally one to three years for IBX space customers. Non-recurring installation fees, although generally paid in a lump sum upon installation, are deferred and recognized ratably over the longer of the term of the related contract or expected customer relationship.

EQUINIX, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Professional service fees are recognized in the period in which the services were provided and represent the culmination of the earnings process as long as they meet the criteria for separate recognition under EITF Abstract No. 00-21, Revenue Arrangements with Multiple Deliverables. Revenue from bandwidth and equipment is recognized on a gross basis in accordance with EITF Abstract No. 99-19, Recording Revenue as a Principal versus Net as an Agent , primarily because the Company acts as the principal in the transaction, takes title to products and services and bears inventory and credit risk. To the extent the Company does not meet the criteria for gross basis accounting for bandwidth and equipment revenue, the Company records the revenue on a net basis. Revenue from contract settlements, which is for when a customer wishes to terminate their contract early, is generally recognized on a cash basis when no remaining performance obligations exist to the extent that the revenue has not previously been recognized.

The Company occasionally guarantees certain service levels, such as uptime, as outlined in individual customer contracts. To the extent that these service levels are not achieved, the Company reduces revenue for any credits given to the customer as a result. The Company generally has the ability to determine such service level credits prior to the associated revenue being recognized, and historically, these credits have generally not been significant. There were no significant service level credits recorded during the three and nine months ended September 30, 2006. During the three and nine months ended September 30, 2005, the Company recorded a total of $247,000 and $607,000, respectively, in service level credits to various customers associated with two separate power outages that affected the Company s Chicago and Washington, D.C. metro area IBX centers.

Revenue is recognized only when the service has been provided and when there is persuasive evidence of an arrangement, the fee is fixed or determinable and collection of the receivable is reasonably assured. It is customary business practice to obtain a signed master sales agreement and sales order prior to recognizing revenue in an arrangement. The Company assesses collection based on a number of factors, including past transaction history with the customer and the credit-worthiness of the customer. The Company generally does not request collateral from its customers although in certain cases the Company obtains a security interest in a customer s equipment placed in its IBX centers or obtains a deposit. If the Company determines that collection of a fee is not reasonably assured, the Company defers the fee and recognizes revenue at the time collection becomes reasonably assured, which is generally upon receipt of cash. In addition, Equinix also maintains an allowance for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments for which the Company had expected to collect the revenues. If the financial condition of Equinix s customers were to deteriorate or if they become insolvent, resulting in an impairment of their ability to make payments, greater allowances for doubtful accounts may be required. Management specifically analyzes accounts receivable and current economic news and trends, historical bad debts, customer concentrations, customer credit-worthiness and changes in customer payment terms when evaluating revenue recognition and the adequacy of the Company s reserves. A specific bad debt reserve of up to the full amount of a particular invoice value is provided for certain problematic customer balances. A general reserve is established for all other accounts based on the age of the invoices and an analysis of historical credits issued. Delinquent account balances are written-off after management has determined that the likelihood of collection is not probable.

Net Loss per Share

The Company computes net loss per share in accordance with SFAS No. 128, Earnings per Share; SEC Staff Accounting Bulletin (SAB) No. 98; EITF Issue 03-6, Participating Securities and the Two-Class Method Under FASB 128; EITF Issue 04-8 The Effect of Contingently Convertible Instruments on Diluted Earnings per Share and SFAS No. 123(R), Share-Based Payment. Under the provisions of SFAS No. 128, SAB No. 98, EITF Issues 03-6 and 04-8 and SFAS No. 123R, basic and diluted net loss per share are computed using the weighted-average number of common shares outstanding. Options, warrants and contingently convertible instruments were not included in the computation of diluted net loss per share. Under EITF Issue 03-6, the Company s preferred stock qualified as a participating security, but was not included in the Company s basic and diluted net loss per share calculations for prior periods as the holder of preferred stock did not have a contractual obligation to share in the Company s losses. In addition, under EITF 04-8, the Company s Convertible Subordinated Debentures qualify as contingently convertible instruments; however, they were not included in the Company s diluted net loss per share calculations because to do so would be anti-dilutive for all periods presented.

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EQUINIX, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table sets forth the computation of basic and diluted net loss per share for the periods presented (in thousands, except per share amounts) (unaudited):

	Three months ended September 30, 2006	Three months ended September 30, 2005	Nine months ended September 30, 2006	Nine months ended September 30, 2005
Numerator:				
Net loss	$ (5,168)	$ (783)	$ (15,508)	$ (10,008)
Denominator:				
Weighted-average shares	28,991	24,076	28,606	23,335
Weighted-average unvested restricted shares issued subject to forfeiture	(248)		(250)	
Total weighted average shares	28,743	24,076	28,356	23,335
Net loss per share:				
Basic and diluted	$ (0.18)	$ (0.03)	$ (0.55)	$ (0.43)

The following table sets forth potential shares of common stock that are not included in the diluted net loss per share calculation above because to do so would be anti-dilutive for the periods indicated (unaudited):

	September 30, 2006	September 30, 2005
Series A preferred stock		1,868,667
Series A preferred stock warrant		965,674
Shares reserved for conversion of convertible secured notes		224,229
Shares reserved for conversion of convertible subordinated debentures	2,183,548	2,183,548
Unvested restricted shares issued subject to forfeiture	247,750	
Common stock warrants	9,490	152,359
Common stock related to stock-based compensation plans	3,935,819	4,482,973

Income Taxes

Income taxes are accounted for under the asset and liability method. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the year in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Valuation allowances are established when necessary to reduce deferred tax assets to the amounts that are expected more likely than not to be realized in the future. The assessment of whether or not a valuation allowance is required often requires significant judgment including the forecast of future taxable income and the evaluation of tax planning strategies in each of the jurisdictions in which the Company operates. The Company also accounts for any income tax contingencies in accordance with SFAS No. 5, Accounting for Contingencies.

The Company is currently in a net deferred tax asset position, which has been fully reserved. The Company will continue to provide a valuation allowance for the net deferred tax asset until it becomes more likely than not that the net deferred tax asset will be realizable. For the three and nine months ended September 30, 2006, the Company recorded a tax provision of $270,000 and $870,000, respectively. For the three and nine months ended September 30, 2005, the Company recorded a tax provision of $164,000

EQUINIX, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

and $553,000, respectively. The tax provision recorded in each of these periods is attributable primarily to federal alternative minimum tax. The Company expects the alternative minimum tax situation to continue throughout the current taxable year based on its financial outlook for the year. The Company has recorded this income tax provision within accounts payable and accrued expenses on the accompanying balance sheets as of September 30, 2006 and December 31, 2005, along with other taxes, such as personal and real property taxes (see Note 6). During the nine months ended September 30, 2006, the Company reduced $825,000 of this income tax payable within accounts payable and accrued expenses, and increased additional paid-in capital as a result of excess tax benefits associated with the stock options exercised by employees during the periods.

Construction in Progress

Construction in progress includes direct and indirect expenditures for the construction and expansion of IBX centers and is stated at original cost. The Company has contracted out substantially all of the construction and expansion efforts of its IBX centers to independent contractors under construction contracts. Construction in progress includes certain costs incurred under a construction contract including project management services, engineering and schematic design services, design development, construction services and other construction-related fees and services. In addition, the Company has capitalized certain interest costs during the construction phase. Once an IBX center or expansion project becomes operational, these capitalized costs are allocated to certain property and equipment categories and are depreciated at the appropriate rates consistent with the estimated useful life of the underlying assets.

Interest incurred is capitalized in accordance with SFAS No. 34, Capitalization of Interest Costs. Total interest cost incurred and total interest capitalized during the three months ended September 30, 2006, was $3,905,000 and $354,000, respectively. During the nine months ended September 30, 2006, total interest cost incurred and total interest capitalized was $12,026,000 and $1,042,000, respectively. There was no interest capitalized during the three and nine months ended September 30, 2005.

Asset Retirement Obligations

SFAS No. 143, Accounting for Asset Retirement Obligations and FASB Interpretation No. 47, Accounting for Conditional Asset Retirement Obligations, an Interpretation of FASB Statement No. 143 establish accounting standards for recognition and measurement of a liability for an asset retirement obligation and the associated asset retirement cost. The fair value of a liability for an asset retirement obligation is to be recognized in the period in which it is incurred if a reasonable estimate of fair value can be made. The associated retirement costs are capitalized and included as part of the carrying value of the long-lived asset and amortized over the useful life of the asset. Subsequent to the initial measurement, the Company is accreting the liability in relation to the asset retirement obligations over time and the accretion expense is being recorded as a cost of revenue. The Company s asset retirement obligations are primarily related to its IBX Centers, of which the majority are leased under long-term arrangements, and, in certain cases, are required to be returned to the landlords in original condition. All of the Company s IBX center leases have been subject to significant development by the Company in order to convert them from, in most cases, vacant buildings or warehouses into IBX centers. The majority of the Company IBX centers initial lease terms expire at various dates ranging from 2010 to 2020 and most of them have renewal options available to the Company.

During the three and nine months ended September 30, 2006, the Company recorded accretion expense related to its asset retirement obligations of $138,000 and $394,000, respectively. During the three and nine months ended September 30, 2005, the Company recorded accretion expense related to its asset retirement obligations of $135,000 and $382,000, respectively. The Company records its asset retirement obligations liability within other liabilities on the accompanying balance sheets (see Note 8).

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EQUINIX, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Stock-Based Compensation

On January 1, 2006, the Company adopted the provisions of, and accounts for stock-based compensation in accordance with, SFAS No. 123(R), Share-Based Payment, and related pronouncements (SFAS 123(R)). The Company elected the modified-prospective method, under which prior periods are not revised for comparative purposes. Under the fair value recognition provisions of this statement, stock-based compensation cost is measured at the grant date for all stock-based awards made to employees and directors based on the fair value of the award using an option-pricing model and is recognized as expense over the requisite service period, which is generally the vesting period. The Company has three types of equity awards or plans, which have been impacted by SFAS 123(R): (i) stock options, (ii) restricted stock with both a service and market price condition and (iii) an employee stock purchase plan (ESPP). SFAS 123(R) supersedes the Company s previous accounting under Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, (APB 25) for periods beginning in fiscal year 2006. In March 2005, the SEC issued Staff Accounting Bulletin No. 107 (SAB 107) providing supplemental implementation guidance for SFAS 123(R). The Company has applied the provisions of SAB 107 in its adoption of SFAS 123(R).

Prior to the adoption of SFAS 123(R), the Company accounted for stock-based awards to employees and directors using the intrinsic value method in accordance with APB 25 as allowed under SFAS No. 123, Accounting for Stock-Based Compensation (SFAS 123). Under the intrinsic value method, no stock-based compensation expense for employee stock options had generally been recognized in the Company s consolidated statements of operations because the exercise price of its stock options granted to employees and directors since the date of the Company s initial public offering generally equaled the fair market value of the underlying stock at the date of grant. The Company did, however, recognize stock-based compensation in connection with its restricted stock grants, granted for the first time in the first quarter of 2005, as these were deemed to be a compensatory plan under the provisions of APB 25 and, as a result, were accounted for as variable awards in the Company s consolidated statements of operation.

The Company currently uses the Black-Scholes option-pricing model to determine the fair value of stock options and shares purchased under the employee stock purchase plan as they only have a service condition. The Company currently uses a Monte Carlo simulation option-pricing model to determine the fair value of its restricted stock grants since they have both a service and market price condition. The determination of the fair value of stock-based payment awards on the date of grant using an option-pricing model is affected by the Company s stock price as well as assumptions regarding a number of complex and subjective variables. These variables include the Company s expected stock price volatility over the term of the awards; actual and projected employee stock option exercise behaviors, which is referred to as expected term; risk-free interest rate and expected dividends.

As a result of the Company s adoption of SFAS 123(R), the Company recorded stock-based compensation expense of $6,885,000 or $0.24 per share and $23,540,000 or $0.83 per share for the three and nine months ended September 30, 2006, respectively; however, had the Company continued to record its stock-based compensation expense under the provisions of APB 25, the recorded stock-based compensation expense would have been approximately $2,049,000 or $0.07 per share and approximately $7,332,000 or $0.26 per share for the three and nine months ended September 30, 2006, respectively. For the three and nine months ended September 30, 2005, the Company recorded stock-based compensation expense in accordance with APB 25 of $1,358,000 and $6,291,000, respectively.

Stock-based compensation expense recognized during a period is based on the value of the portion of stock-based awards that is ultimately expected to vest during the period. Stock-based compensation expense recognized in the three and nine months ended September 30, 2006 included compensation expense for stock-based awards granted prior to, but not yet vested, as of December 31, 2005, based on the fair value on the grant date estimated in accordance with the pro forma provisions of SFAS 123, and compensation expense for the stock-based awards granted subsequent to December 31, 2005, based on the fair value on the grant date estimated in accordance with the provisions of SFAS 123(R). In conjunction with the adoption of SFAS 123(R), the Company changed its method of attributing the value of stock-based compensation expense from the accelerated multiple-option method to the ratable single-option method for

EQUINIX, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

stock options and its ESPP; however, restricted stock grants will continue to be amortized over the accelerated multiple-option method due to their market price condition. Compensation expense for all stock-based awards granted on or prior to December 31, 2005, will continue to be recognized using the accelerated multiple-option approach, while compensation expense for all stock-based awards granted subsequent to December 31, 2005, will be recognized using the straight-line single-option method (except for restricted stock as discussed above). Stock-based compensation expense recognized in the Company s results for the three and nine months ended September 30, 2006 is based on awards ultimately expected to vest; it has been reduced for estimated forfeitures. SFAS 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. The Company uses historical data to estimate pre-vesting option forfeitures. Prior to fiscal year 2006, the Company accounted for forfeitures as they occurred for the purposes of pro forma information under SFAS 123 and for any stock-based compensation that the Company recorded to its statements of operations under APB 25.

The Company estimates the expected term of options granted by taking the average of the vesting term and the contractual term of the option, as illustrated in SAB 107. The Company estimates the volatility of its common stock by using its historical volatility that the Company believes best represents its future volatility in accordance with SAB 107. The Company bases the risk-free interest rate that it uses in its option-pricing models on U.S. Treasury zero-coupon issues with remaining terms similar to the expected term on its equity awards. The Company does not anticipate paying any cash dividends in the foreseeable future and therefore used an expected dividend yield of zero in its option-pricing models. Generally, stock options granted prior to October 1, 2005 have a contractual term of ten years from the date of grant, and stock options granted on or after October 1, 2005 have a contractual term of seven years from the date of grant.

On November 10, 2005, the FASB issued FASB Staff Position No. FAS 123(R)-3, Transition Election Related to Accounting for Tax Effects of Share-Based Payment Awards, that allows for a simplified method to establish the beginning balance of the APIC pool related to the tax effects of employee stock-based compensation, and to determine the subsequent impact on the APIC pool and consolidated statements of cash flows of the tax effects of employee stock-based compensation awards that are outstanding upon adoption of SFAS 123(R). The Company is still in the process of calculating the APIC pool and has not yet determined if it will elect to adopt the simplified method.

If factors change and the Company employs different assumptions for estimating stock-based compensation expense in future periods or if it decides to use a different valuation model in the future, the future periods may differ significantly from what the Company has recorded in the current period and could materially affect its operating results, net income or loss and net income or loss per share.

For further information on stock-based compensation, see Note 10 below.

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EQUINIX, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Goodwill and Other Intangible Assets

Goodwill and other intangible assets, net, consisted of the following (in thousands):

	September 30, 2006 (unaudited)	December 31, 2005
Goodwill	$ 22,710	$ 21,654
Other intangibles:		
Intangible asset customer contracts	4,234	4,051
Intangible asset leases	1,017	
Intangible asset tradename	328	313
Intangible asset workforce	160	160
Intangible asset lease expenses	111	
	5,850	4,524
Accumulated amortization	(5,185)	(4,349)
	665	175
	$ 23,375	$ 21,829

The Company s goodwill is an asset denominated in Singapore dollars. As a result, it is subject to foreign currency fluctuations. The Company s foreign currency translation gains and losses are a component of other comprehensive income and loss (see Note 13).

During the three months ended March 31, 2006, the Company finalized its accounting for the Ashburn Campus Property Acquisition from the fourth quarter of 2005 and, as a result, reduced property and equipment by $1,128,000, offset by an increase in several intangible assets in connection with various leases acquired from multiple tenants on the Ashburn Campus totaling $1,128,000. The Company amortizes these other identifiable intangible assets on a straight-line basis over their estimated useful lives. Other intangible assets, net, are included in other assets on the accompanying balance sheets as of September 30, 2006 and December 31, 2005.

For the three and nine months ended September 30, 2006, the Company recorded amortization expense of $160,000 and $638,000, respectively. For the three and nine months ended September 30, 2005, the Company recorded amortization expense of $15,000 and $45,000, respectively. The Company expects to record the following amortization expense during 2006 and beyond (in thousands) (unaudited):

Year ending:	
2006 (three months remaining)	$ 143
2007	237
2008	180
2009	67
2010	38
Total	$ 665

2. IBX Acquisitions and Expansions

Washington, D.C. Metro Area IBX Expansion Project

In February 2006, the Company announced its intention to build out a new IBX center within the Ashburn Campus in order to further expand its existing Washington, D.C. metro area IBX center (the Washington, D.C. Metro Area IBX Expansion Project). In May 2006, the Company began new construction to build out one of the undeveloped buildings located on the Ashburn Campus for a cost of approximately $60,000,000, of which approximately $56,000,000 is expected to be incurred in 2006. The

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EQUINIX, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

center will feature an updated design that will enable the Company to support the increased power and cooling demands of customers. The Company intends to open the new center for customers during the three months ending March 31, 2007. The Washington, D.C. Metro Area IBX Expansion Project will fulfill the Company s obligation to invest at least $40,000,000 in capital improvements to the Ashburn Campus by December 31, 2007 pursuant to the terms of the Mortgage Payable on its Ashburn Campus. In September 2006, the Company received loan commitments, subject to customary closing conditions, for $40,000,000 to finance this Washington, D.C. Metro Area IBX Expansion Project in a long-term financing arrangement at anticipated rates of approximately 8%, which the Company expects to close during the fourth quarter of 2006. In September 2006, the Company elected to borrow $40,000,000 from the Silicon Valley Bank Credit Line Amendment to partially finance this project (see Note 9).

Chicago Metro Area IBX Expansion Project

In June 2006, the Company purchased a 228,000 square foot stand-alone office/warehouse complex for $9,766,000, including closing costs in a cash transaction in June 2006. The Company intends to build an IBX center, which will be the company s second IBX center location in the Chicago Metro Area, in multiple phases (the Chicago Metro Area IBX Expansion Project). This new IBX center will be interconnected to the Company s existing downtown Chicago IBX centers through redundant dark fiber links managed by the Company. The Company plans to invest approximately $165,000,000 to build out the first phase, of which approximately $40,000,000 is expected to be incurred in 2006. This includes an investment of approximately $40,000,000 to construct a specially built 250,000 square foot shell, acquire access to power and provision fiber for interconnection to the Company s downtown Chicago IBX center location. The site development plan allows a second expansion phase at an incremental investment of $30,000,000. The Company intends to open the new center for customers during the three months ended September 30, 2007. In September 2006, the Company received loan commitments, subject to customary closing conditions, for $110,000,000 to finance at least 60% of the construction costs or a maximum of $110,000,000 in a long-term financing arrangement at anticipated rates of approximately 8%, which the Company expects to close during the fourth quarter of 2006. In September 2006, the Company elected to borrow $40,000,000 from the Silicon Valley Bank Credit Line Amendment to partially finance this project (see Note 9).

New York Metro Area IBX Expansion Project

In September 2006, the Company entered into a long-term lease for a 340,000 square foot building in the New York metro area. The Company intends to build an IBX center, which will be the Company s fourth IBX center in the New York metro area, and this new center will be interconnected to the Company s existing IBX centers in the New York metro area through redundant dark fiber links managed by the Company (the New York Metro Area IBX Expansion Project). Payments under this lease total $59,410,000, which will be paid in monthly installments through September 2021. The lease, which commenced in October 2006, contains a three-year option to purchase the building for $39,000,000. The Company intends to build out the new center in multiple phases and expects to open the first phase for customers during the three months ended September 30, 2007. As previously announced, the Company intends to invest approximately $80,000,000 to $90,000,000 to build out the first phase of the new center, of which approximately $4,000,000 is expected to be incurred in 2006. The Company expects to finance at least 60% of the capital expenditures required to complete the New York Metro Area IBX Expansion Project in the form of short and long-term financing arrangements, which it expects to obtain in 2007.

3. Related Party Transactions

A significant amount of the Company s Asia-Pacific revenues are generated in Singapore and a significant portion of the business in Singapore is transacted with entities affiliated with STT Communications, which is the Company s single largest stockholder. For the three and nine months ended September 30, 2006, revenues recognized with related parties, primarily entities affiliated with STT Communications, were $1,279,000 and $4,117,000, respectively, and as of September 30, 2006, accounts receivable with these related parties was $1,062,000. For the three and nine months ended September 30,

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2006, costs and services procured with related parties, primarily entities affiliated with STT Communications, were $864,000 and $2,883,000, respectively, and as of September 30, 2006, accounts payable with these related parties was $283,000. For the three and nine months ended September 30, 2005, revenues recognized with related parties, primarily entities affiliated with STT Communications, were $1,344,000 and $4,625,000, respectively, and as of September 30, 2005, accounts receivable with these related parties was $875,000. For the three and nine months ended September 30, 2005, costs and services procured with related parties, primarily entities affiliated with STT Communications, were $744,000 and $2,240,000, respectively, and as of September 30, 2005, accounts payable with these related parties was $354,000.

4. Accounts Receivable

Accounts receivables, net, consisted of the following (in thousands):

	September 30, 2006 (unaudited)	December 31, 2005
Accounts receivable	$ 48,631	$ 36,430
Unearned revenue	(24,222)	(19,048)
Allowance for doubtful accounts	(280)	(145)
	$ 24,129	$ 17,237

Trade accounts receivable are recorded at the invoiced amount and do not bear interest. Unearned revenue consists of pre-billing for services that have not yet been provided, but which have been billed to customers in advance in accordance with the terms of their contract.

5. Property and Equipment

Property and equipment consisted of the following (in thousands):

	September 30, 2006 (unaudited)	December 31, 2005
Leasehold improvements	$ 416,729	$ 395,698
IBX plant and machinery	178,540	146,896
IBX equipment	81,775	63,786
Computer equipment and software	40,283	26,253
Buildings	50,526	51,280
Land	24,967	15,415
Furniture and fixtures	2,544	2,218
Construction in progress	47,435	17,271
	842,799	718,817
Less accumulated depreciation	(342,882)	(280,027)
	$ 499,917	$ 438,790

Leasehold improvements, IBX plant and machinery, computer equipment and software and buildings recorded under capital leases aggregated $35,309,000 at both September 30, 2006 and December 31, 2005. Amortization on the assets recorded under capital leases is included in depreciation expense and accumulated depreciation on such assets totaled $4,119,000 and $2,354,000 as of September 30, 2006 and December 31, 2005, respectively.

As of September 30, 2006 and December 31, 2005, the Company had accrued property and equipment of $18,597,000 and $15,783,000, respectively. The Company s planned capital expenditures during the remainder of 2006 and 2007 in connection with recently acquired IBX properties and expansion efforts are substantial. For further information, refer to Other Purchase Commitments in Note 12.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

6. Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses consisted of the following (in thousands):

	September 30, 2006 (unaudited)	December 31, 2005
Accounts payable	$ 2,420	$ 3,337
Accrued compensation and benefits	8,855	8,632
Accrued taxes	3,100	3,571
Accrued utility and security	3,958	3,420
Accrued professional fees	2,039	1,303
Accrued interest	682	873
Accrued other	1,953	1,421
	$ 23,007	$ 22,557

7. Other Current Liabilities

Other current liabilities consisted of the following (in thousands):

	September 30, 2006 (unaudited)	December 31, 2005
Deferred installation revenue, current	$ 6,843	$ 6,324
Customer deposits	825	868
Deferred rent, current	408	399
Other current liabilities	441	381
	$ 8,517	$ 7,972

8. Deferred Rent and Other Liabilities

Deferred rent and other liabilities consisted of the following (in thousands):

	September 30, 2006 (unaudited)	December 31, 2005
Deferred rent, non-current	$ 20,710	$ 18,392
Asset retirement obligations	4,043	3,649
Deferred installation revenue, non-current	2,835	1,334
Other liabilities	291	351

	$ 27,879	$ 23,726

The Company currently leases the majority of its IBX centers and certain equipment under non-cancelable operating lease agreements expiring through 2025. The centers lease agreements typically provide for base rental rates that increase at defined intervals during the term of the lease. In addition, the Company has negotiated rent expense abatement periods to better match the phased build-out of its centers. The Company accounts for such abatements and increasing base rentals using the straight-line method over the life of the lease. The difference between the straight-line expense and the cash payment is recorded as deferred rent.

9. Debt Facilities and Other Financing Obligations

Silicon Valley Bank Credit Line

In January 2006, the Company fully repaid the $30,000,000 Borrowing from the Silicon Valley Bank Credit Line. In August 2006, the Company amended the Silicon Valley Bank Credit Line to increase the line

EQUINIX, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

to $75,000,000, replacing the previously outstanding $50,000,000 line of credit arrangement with the same bank, and added General Electric Capital Corporation (GE) as a lender (the Silicon Valley Bank Credit Line Amendment). The Silicon Valley Bank Credit Line Amendment allows for issuance of letters of credit (in addition to revolving borrowings). The Silicon Valley Bank Credit Line Amendment also has an option for the Company to increase the amount of the line to $100,000,000 at a later date, subject to approval of the lender or lenders electing to participate in such increase. Borrowings under the Silicon Valley Bank Credit Line Amendment will continue to bear interest at variable interest rates, plus the applicable margins, which were in effect prior to the amendment, based on either prime rates or LIBOR rates. The Silicon Valley Bank Credit Line Amendment matures on September 15, 2008 and is secured by substantially all of the Company s domestic personal property assets and certain of the Company s real property leases and contains several financial covenants, which require compliance with maximum leverage and working capital ratios and a minimum EBITDA target, all of which the Company was in compliance with as of September 30, 2006.

In September 2006, the Company elected to borrow $40,000,000 (the $40,000,000 Borrowing) from the Silicon Valley Bank Credit Line Amendment, of which $20,000,000 of the $40,000,000 Borrowing was borrowed at the prime rate and bears interest at 8.75% per annum and the remaining $20,000,000 was borrowed at a spread over the one-month LIBOR rate and bears interest at 7.824% per annum. The $40,000,000 Borrowing was used to fund capital expenditures and construction costs related to the Washington D.C. Metro Area IBX Expansion Project and Chicago Metro Area IBX Expansion Project. As of September 30, 2006, the $40,000,000 Borrowing from Silicon Valley Bank Credit Line Amendment had an effective blended interest rate of 8.29% per annum.

As of September 30, 2006, in addition to the $40,000,000 Borrowing, the Company had also utilized $6,700,000 under the letters of credit sublimit with the issuance of five letters of credit under the Silicon Valley Bank Credit Line Amendment reducing the amount of borrowings available to the Company from $75,000,000 to $28,300,000. These letters of credit automatically renew in successive one-year periods until the final lease expiration dates. If the landlords for any of these five IBX leases decide to draw down on these letters of credit, the Company will be required to fund these letters of credit either through cash collateral or borrowings under the Silicon Valley Bank Credit Line Amendment.

At the time the Company entered into the Silicon Valley Bank Credit Line Amendment, a total of $321,000 of issuance costs remained unamortized related to the Silicon Valley Bank Credit Line. In addition, the Company incurred $253,000 of additional issuance costs to secure the Silicon Valley Bank Credit Line Amendment. In accordance with EITF Issue 98-14, Debtor s Accounting for Changes in Line-of-Credit or Revolving-Debt Arrangements , the Company has capitalized the total of such issuance costs, which are being amortized to interest expense using the effective interest method over the life of the Silicon Valley Bank Credit Line Amendment. These debt issuance costs, net of amortization, were $529,000 as of September 30, 2006.

In October 2006, the Company utilized an additional $7,800,000 under the letters of credit sublimit associated with the Silicon Valley Bank Credit Line Amendment in connection with the new lease for the New York Metro Area IBX Expansion Project and fully repaid the $40,000,000 Borrowing (see Note 17).

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Maturities

Combined aggregate maturities for the Company s various debt facilities and other financing obligations as of September 30, 2006 are as follows (in thousands) (unaudited):

	Capital lease and other financing obligations	Mortgage payable	Borrowings under credit line and convertible subordinated debentures	Total
2006 (three months remaining)	$ 2,348	$ 1,505	$ 40,000	$ 43,853
2007	9,568	6,022		15,590
2008	9,842	6,022		15,864
2009	10,122	6,022	86,250	102,394
2010	10,409	6,022		16,431
2011 and thereafter	128,354	90,838		219,192
	170,643	116,431	126,250	413,324
Less amount representing interest	(82,123)	(57,266)		(139,389)
Plus amount representing residual property value	6,555			6,555
	95,075	59,165	126,250	280,490
Less current portion of principal	(1,855)	(1,337)	(40,000)	(43,192)
	$ 93,220	$ 57,828	$ 86,250	$ 237,298

10. Stockholders Equity and Stock-Based Compensation

The Company s employee stock plans are a long-term retention program that is intended to attract, retain and provide incentives for talented employees, officers and directors, and to align stockholder and employee interests. The Company considers its stock plans to be critical for its operation and productivity and essentially all of the Company s employees participate. The Company s stock plans are described below.

Stock Option Plans

In May 2000, the Company s stockholders approved the adoption of the 2000 Equity Incentive Plan as the successor plan to the 1998 Stock Plan. In August 2000 the Company no longer issued additional grants under the 1998 Stock Plan, and unexercised options under the predecessor 1998 Stock Plan that cancel due to an optionee s termination may be reissued under the successor 2000 Equity Incentive Plan. Under the 2000 Equity Incentive Plan, nonstatutory stock options, restricted shares, restricted stock units, and stock appreciation rights may be granted to employees, outside directors and consultants at not less than 85% of the fair market value on the date of grant, and incentive stock options may be granted to employees at not less than 100% of the fair market value on the date of grant. Options granted prior to October 1, 2005 generally expire 10 years from the grant date, and options granted to employees and consultants on or after October 1, 2005 will generally expire seven years from the grant date, subject to continuous service of the optionee. Stock options and restricted shares granted under the 2000 Equity Incentive Plan generally vest over four years. As of September 30, 2006, the Company has reserved a total of 8,219,601 shares for issuance under the 2000

Equity Incentive Plan of which 1,685,475 were still available for grant, and the plan reserve is increased on January 1 each year by the lesser of 6% of the common stock then outstanding or 6,000,000 shares. The 2000 Equity Incentive Plan is administered by the Compensation Committee of the Board of Directors, and the Board may terminate or amend the plan, with approval of the stockholders as may be required by applicable regulations, at any time.

In May 2000, the Company s stockholders approved the adoption of the 2000 Director Option Plan, which was amended and restated effective January 1, 2003. Under the 2000 Director Option Plan, each non-employee board member who was not previously an employee of the Company will receive an automatic initial nonstatutory stock option to purchase 7,000 shares (in addition to an option for 8,000 shares if chairperson of the Compensation or Nominating Committees, or 13,000 if chairperson of the Audit Committee, granted from the 2000 Equity Incentive Plan), which vests in four annual installments. In

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

addition, each non-employee board member will receive an annual nonstatutory stock option to purchase 2,500 shares (in addition to an option to purchase 2,500 shares granted from the 2000 Equity Incentive Plan) on the date of the Company s regular Annual Meeting of Stockholders, provided the board member will continue to serve as a director thereafter. Such annual option shall vest in full on the earlier of a) the first anniversary of the grant, or b) the date of the regular Annual Meeting of Stockholders held in the year following the grant date. A new director who receives an initial option will not receive an annual option in the same calendar year. Options granted under the 2000 Director Option Plan will have an option price not less than 100% of the fair market value on the date of grant and will have a 10-year contractual term, subject to continuous service of the board member. As of September 30, 2006, the Company has reserved 393,440 shares subject to options for issuance under the 2000 Director Option Plan of which 335,938 were still available for grant, and an additional 50,000 shares is added to the reserve on January 1 each year. The 2000 Director Option Plan is administered by the Compensation Committee of the Board of Directors, and the Board may terminate or amend the plan, with approval of the stockholders as may be required by applicable regulations, at any time.

In September 2001, the Company adopted the 2001 Supplemental Stock Plan, under which non-statutory stock options and restricted shares may be granted to consultants and employees who are not executive officers or board members, at not less than 85% of the fair market value on the date of grant. Options granted prior to October 1, 2005 generally expire 10 years from the grant date, and options granted on or after October 1, 2005 will generally expire seven years from the grant date, subject to continuous service of the optionee. Current stock options granted under the 2001 Supplemental Stock Plan generally vest over four years. As of September 30, 2006, the Company has reserved a total of 1,493,961 shares for issuance under the 2001 Supplemental Stock Plan, of which 160,479 were still available for grant. The 2001 Supplemental Stock Plan is administered by the Compensation Committee of the Board of Directors, and the plan will continue in effect indefinitely unless the Board decides to terminate it earlier.

The 1998 Stock Plan, 2000 Equity Incentive Plan, 2000 Director Option Plan and 2001 Supplemental Stock Plan are collectively referred to as the Stock Option Plans.

Stock Option Plan Activity

Stock option activity under the Stock Option Plans is summarized as follows (unaudited):

	Number of shares outstanding	Weighted-average exercise price per share
Stock options outstanding at December 31, 2005	4,162,539	$ 33.67
Stock options granted	1,104,385	53.58
Stock options exercised	(1,253,011)	19.83
Stock options forfeited	(373,882)	39.82
Stock options expired	(18,428)	130.55
Stock options outstanding at September 30, 2006	3,621,603	43.41

The total intrinsic value of stock options exercised during the three and nine months ended September 30, 2006 was $7,013,000 and $41,204,000, respectively. The intrinsic value is calculated as the difference between the market value on the date of exercise and the exercise price of the shares. The total fair value of options vested during the three and nine months ended September 30, 2006 was $10,785,000 and $26,981,000, respectively.

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The following table summarizes information about outstanding equity awards as of September 30, 2006 (unaudited):

	Outstanding			Exercisable	
Range of exercise prices	Number of shares	Weighted-average remaining contractual life	Weighted-average exercise price	Number of shares	Weighted-average exercise price
$2.13 to $17.70	512,484	6.55	$ 10.43	505,208	$ 10.48
$18.61 to $29.80	450,910	6.96	27.37	263,657	27.46
$30.00 to $30.02	379,512	7.36	30.02	228,708	30.02
$30.38 to $40.74	390,727	7.03	36.88	106,781	36.12
$40.83 to $44.70	240,163	8.48	42.18	76,799	42.15
$44.89 to $44.89	417,783	8.31	44.89	146,779	44.89
$45.08 to $52.51	156,108	6.55	48.17	5,901	50.24
$52.85 to $52.85	591,238	6.41	52.85	96,721	52.85
$53.09 to $72.00	285,340	6.80	58.94	21,155	57.50
$85.33 to $384.00	197,338	3.82	148.17	197,338	148.17
	3,621,603	6.92	43.41	1,649,047	41.81

The total aggregate intrinsic value of stock options outstanding and stock options exercisable as of September 30, 2006 was $78,121,000 and $36,495,000, respectively. As of September 30, 2006, the weighted average remaining contractual life of options outstanding and exercisable was 6.92 years and 6.51 years, respectively. The market value as of September 30, 2006 was $60.10 as reported by the Nasdaq National Market System. Cash proceeds from the exercises of stock options were $24,843,000 and $6,309,000 for the nine months ended September 30, 2006 and 2005, respectively.

Fair Value Calculations Stock Options

The Company uses the Black-Scholes option-pricing model to determine the fair value of stock options. The assumptions used to value stock option were as follows (unaudited):

	Three months ended September 30,		Nine months ended September 30,	
	2006	2005	2006	2005
Dividend yield	0%	0%	0%	0%
Expected volatility	68%	75%	70%	79%
Risk-free interest rate	4.79%	4.04%	4.72%	3.93%
Expected life (in years)	4.58	4.00	4.56	4.00

The weighted-average fair value of stock options per share on the date of grant was $32.44 and $31.66, respectively, for the three and nine months ended September 30, 2006. The weighted-average fair value of stock options per share on the date of grant for the three and nine months ended September 30, 2005 was $23.67 and $25.39, respectively.

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Restricted Share Activity

As noted above, the Company grants restricted shares out of the 2000 Equity Incentive Plan. Restricted Share activity under the 2000 Equity Incentive Plan is summarized as follows (unaudited):

	Number of shares outstanding	Weighted-average grant date fair value per share
Restricted shares outstanding, December 31, 2005	280,438	$ 43.76
Restricted shares granted	274,000	44.43
Restricted shares issued, unvested (1)	(274,000)	44.43
Restricted shares issued, vested	(69,313)	43.76
Restricted shares canceled	(51,125)	43.76
Restricted shares outstanding, September 30, 2006 (2)	160,000	43.76

(1) On January 10, 2006 and May 22, 2006, the Company granted 250,000 restricted shares and 24,000 restricted shares, respectively, to its executive officers and at the same time, unlike the previous year s restricted stock grants (see footnote 2 below), issued these shares into an escrow account under the names of each of the executive officers. These shares have voting rights and are considered issued and outstanding. They are released from the escrow account as they vest. However, they are subject to forfeiture if the individual officers do not meet the vesting requirements. See Net Loss Per Share in Note 1.

(2) As of September 30, 2006, there was a total of 160,000 restricted shares outstanding and unissued. These restricted shares were granted on February 8, 2005 to the Company s executive officers. These shares were not placed into an escrow account in the names of each of the executive officers. These shares do not have voting rights and are not considered issued and outstanding. These restricted shares will only be issued when they become vested.

Unvested restricted shares as of December 31, 2005 totaled 280,438. Unvested restricted shares as of September 30, 2006 totaled 407,750 comprised of 247,750 issued shares and 160,000 unissued shares.

Fair Value Calculations Restricted Shares

The Company uses a Monte Carlo simulation option-pricing model to determine the fair value of restricted shares as they have both a service and market price condition. The assumptions used to value restricted shares were as follows (unaudited):

	Three months ended September 30,		Nine months ended September 30,	
	2006	2005	2006	2005
Dividend yield			0%	0%
Expected volatility			71%	80%
Risk-free interest rate			4.43%	3.55%

Market risk premium	8.5%	8.5%
Beta	1.28	1.28

The weighted-average fair value per share of restricted shares on the date of grant was $44.43 for the nine months ended September 30, 2006.

Employee Stock Purchase Plans

In May 2000, the Company adopted the 2000 Employee Stock Purchase Plan (the 2000 Purchase Plan) under which 31,250 shares were reserved for issuance, and after January 1, 2005, no additional shares were added to the 2000 Purchase Plan. The last purchase under the 2000 Purchase Plan was in July 2005, at which time the 2000 Purchase Plan ceased and the unused reserved shares expired.

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In June 2004, the Company s stockholders approved the adoption of the 2004 Employee Stock Purchase Plan and International Employee Stock Purchase Plan (the 2004 Purchase Plans , collectively with the 2000 Purchase Plan, the Purchase Plans) as successor plans to the 2000 Purchase Plan. A total of 500,000 shares have been reserved for issuance under the 2004 Purchase Plans, and the number of shares available for issuance under the 2004 Purchase Plans automatically increases on January 1 each year beginning in 2005 by the lesser of 2% of the shares of common stock then outstanding or 500,000 shares. As of September 30, 2006, a total of 1,160,584 shares remain available for purchase under the Purchase Plans. The 2004 Purchase Plans permit eligible employees to purchase common stock on favorable terms via payroll deductions, up to 15% of the employee s cash compensation, subject to certain share and statutory dollar limits. Two overlapping offering periods commence during each calendar year, on each February 14 and August 14 or such other periods or dates as determined by the Compensation Committee from time to time, and the offering periods last up to 24 months with a purchase date every six months. The price of each share purchased is 85% of the lower of a) the fair market value per share of common stock on the last trading day before the commencement of the applicable offering period or b) the fair market value per share of common stock on the purchase date. The 2004 Purchase Plans are administered by the Compensation Committee of the Board of Directors, and such plans will terminate automatically in June 2014 unless a) the 2004 Purchase Plans are extended by the Board of Directors and b) the extension is approved within 12 months by the Company s stockholders.

For the three and nine months ended September 30, 2006, 67,638 and 135,325 shares, respectively, were issued under the Purchase Plans at a weighted average purchase price of $29.14 and $28.91 per share, respectively. For the three and nine months ended September 30, 2005, 77,401 and 218,158 shares, respectively, were issued under the Purchase Plans at a weighted average purchase price of $22.94 and $15.62 per share, respectively. Cash proceeds from the issuance of stock under Employee Stock Purchase Plans were $3,913,000 and $3,408,000 for the nine months ended September 30, 2006 and 2005, respectively.

Fair Value Calculations Employee Stock Purchase Plans

The Company uses the Black-Scholes option-pricing model to determine the fair value of shares purchased under the Purchase Plans. The assumptions used to value shares purchased under the Purchase Plans were as follows (unaudited):

	Three months ended September 30,		Nine months ended September 30,	
	2006	2005	2006	2005
Dividend yield	0%	0%	0%	0%
Expected volatility	68%	75%	69%	76%
Risk-free interest rate	5.03%	3.33%	4.95%	3.27%
Expected life (in years)	1.25	1.25	1.25	1.25

The weighted-average fair value per share of shares purchased on the date of purchase was $18.88 and $18.10, respectively, for the three and nine months ended September 30, 2006. For the three and nine months ended September 30, 2005, the weighted-average fair value per share of shares purchased on the date of purchase was $14.60 and $9.65, respectively.

Cumulative Effect Adjustments Under SFAS 123(R)

Upon adoption of SFAS 123(R) on January 1, 2006, the Company recorded the following two cumulative effect adjustments:

For awards with compensation cost recognized in the financial statements under APB 25 that were partially vested upon the adoption of SFAS 123(R), an adjustment to record estimated forfeitures was recorded as a cumulative effect adjustment upon a change in accounting principle totaling $0 and $376,000 in the Company s consolidated statement of operations for the three and nine months ended September 30, 2006, respectively.

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For deferred stock-based compensation related to equity awards granted prior to the adoption of SFAS 123(R), such amounts were eliminated against additional paid-in capital upon adoption, which for the Company totaled $4,930,000 as of December 31, 2005.

Stock-Based Compensation Recognized in the Statement of Operations

The following table presents, by operating expense, the Company s stock-based compensation expense recognized in the Company s consolidated statement of operations under SFAS 123(R) for the three and nine months ended September 30, 2006 and under APB 25 for the three and nine months ended September 30, 2005 (in thousands) (unaudited):

	Three months ended September 30,		Nine months ended September 30,	
	2006	2005	2006	2005
Cost of revenues	$ 664	$	$ 2,385	$
Sales and marketing	1,623	248	5,647	1,149
General and administrative	4,598	1,110	15,508	5,142
	$ 6,885	$ 1,358	$ 23,540	$ 6,291

As of September 30, 2006, the total stock-based compensation cost related to unvested equity awards not yet recognized, net of estimated forfeitures, totaled $48,293,000, which is expected to be recognized over a weighted-average period of 2.6 years.

Pro Forma Stock-Based Compensation Under SFAS 123 for Periods Prior to Fiscal 2006

The following table presents what the net loss and net loss per share would have been had the Company adopted SFAS 123 for the three and nine months ended September 30, 2005 (in thousands, except per share data) (unaudited):

	Three months ended September 30, 2005	Nine months ended September 30, 2005
Net loss as reported	$ (783)	$ (10,008)
Stock-based compensation expense included in net loss	1,358	6,291
Stock-based compensation expense if SFAS No. 123 had been adopted	(7,404)	(27,806)
Pro forma net loss	$ (6,829)	$ (31,523)
Basic and diluted net loss per share:		
As reported	$ (0.03)	$ (0.43)
Pro forma	(0.28)	(1.35)

11. Stock Option Granting Practices

In June 2006, the Audit Committee of the Company s Board of Directors commenced an independent investigation of the Company s historical stock option granting practices and related accounting with the assistance of independent outside legal counsel. This review covers the timing and pricing of all stock option grants made under the Company s stock option plans since August 11, 2000, the day after the Company s Initial Public Offering (IPO).

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EQUINIX, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

As previously announced on June 12, 2006, the Company is currently cooperating with the SEC regarding the SEC s informal inquiry requesting documents related to the Company s stock option grants and practices. The Company also announced on June 29, 2006 that it received a grand jury subpoena from the U.S. Attorney for the Northern District of California and is cooperating fully with the U.S. Attorney s Office in connection with this subpoena. The subpoena requests documents relating to the Company s stock option grants and practices.

Based on the results of its review, the Audit Committee determined that the accounting measurement dates of certain stock option grants issued in the past differ from the actual grant dates. The Audit Committee concluded that the Company did not engage in intentional or fraudulent misconduct in the granting of stock options. However, the accounting measurement dates for certain historical stock option grants differed from their actual grant dates. As a result of revising the accounting measurement dates for these stock option grants, the Company has recorded an additional non-cash stock-based compensation charge totaling $444,000 in the Company s consolidated financial statements for the nine month period ended September 30, 2006. The amount of the charge was computed pursuant to the requirements of APB 25 for all historical periods through December 31, 2005 and pursuant to SFAS 123(R) for the three month period ended March 31, 2006. This $444,000 stock-based compensation charge represents the total charge for historical periods that the Company needed to record as a result of the Audit Committee s conclusion on this matter. This compensation charge has no effect on the Company s current cash position.

The Company concluded that the cumulative charge as a result of the difference between the measurement dates used for financial accounting and reporting purposes and the actual grant dates for certain stock option grants, totaling $444,000, was not material to any previously-reported historical period nor is it expected to be material to the current fiscal year. As such, this cumulative charge totaling $444,000 was recorded in the quarter ended June 30, 2006 and is included in the statement of operations for the nine months ended September 30, 2006, versus restating prior periods. This additional stock-based compensation was combined with the Company s stock-based compensation recorded in connection with FASB 123(R) for the nine months ended September 30, 2006 as outlined in Footnote 10. As of September 30, 2006, the total remaining incremental stock-based compensation charge related to these stock option grants with a revised accounting measurement date not yet recognized, net of estimated forfeitures, totaled approximately $14,000, which is expected to impact the Company s operating results through 2008.

The following table presents, by operating expense category, the Company s cumulative stock-based compensation charge totaling $444,000 recognized in the Company s consolidated statement of operations for the nine months ended September 30, 2006 (in thousands) (unaudited):

Cost of revenues	$ 63
Sales and marketing	99
General and administrative	282
	$ 444

There were no significant income tax effects relating to this adjustment for the Company. However, the Company is currently assessing if any negative tax consequences will impact the Company s employees as a result of this matter. When this determination is reached, the Company may decide to compensate the impacted employees in an amount sufficient to offset any negative tax consequences that they may incur. However, a final decision on this matter will not be made until the Internal Revenue Service provides additional guidance regarding Section 409A of the Internal Revenue Code, which is expected to occur later this year. Any such compensation that the Company elects to make to the employees for any negative tax effects would be recorded at the time that management, including the Board of Directors, makes that election or agrees to such a plan.

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EQUINIX, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

12. Commitments and Contingencies

Legal Matters Relating to Stock Option Granting Practices

In June 2006, the Company received an informal inquiry from the Securities and Exchange Commission (SEC) and a grand jury subpoena from the U.S. Attorney from the Northern District of California (U.S. Attorney) requesting documents relating to its stock option grants and practices. Such inquiries are believed to be related to recent widespread investigations into the practices of public companies relating to the timing of option grants. The Company intends to fully cooperate in all government investigations.

On June 29, 2006 and September 18, 2006, shareholder derivative complaints were filed in the Superior Court of the State of California, County of San Mateo against certain of the Company s current and former officers and directors (the Defendants). The complaints allege that the Defendants breached their fiduciary duties by engaging in allegedly improper stock option grant practices since at least 2000, and by failing to adequately disclose such transactions. The complaints seek unspecified monetary damages, corporate governance changes and restitution. On October 13, 2006, a third shareholder derivative complaint related to allegedly improper stock option grant practices was filed in the United States District Court for the Northern District of California against certain of the Company s current and former officers and directors. The complaint seeks unspecified monetary and punitive damages, corporate governance changes, and the imposition of a constructive trust over certain stock options and related proceeds. At the appropriate time, the Company expects to file motions to dismiss these lawsuits due to the plaintiffs unexcused failure to make a demand on the Company before filing the actions. In addition to the current derivative claims, the Company may be subject to additional derivative or other lawsuits that may be presented on an individual or class basis alleging claims based on its stock option granting practices. Similar lawsuits and investigations have been commenced against numerous other companies based on similar allegations.

Responding to, investigating and/or defending against civil litigations and government inquiries regarding the Company s stock option grants and practices will present a substantial cost to the Company in both cash and the attention of certain management and may have a negative impact on its operations. In addition, in the event of any negative finding or assertion by the SEC, U.S. Attorney, court of law or any third party claim related to the Company s stock option granting practices, the Company may be liable for damages, fines or other civil or criminal remedies or remedial actions, or be required to restate its prior period financial statements or adjust its current period financial statements. Any such adverse action could have a material adverse effect on the Company s business and current market value.

The Company notes that while an unfavorable outcome to any or all of the above-mentioned inquiries, cases or complaints is reasonably possible, the amount of loss, if any, cannot be reasonably estimated at this time. As a result, the Company has not accrued for any settlements in connection with these legal matters as of September 30, 2006.

Other Legal Actions

On July 30, 2001 and August 8, 2001, putative shareholder class action lawsuits were filed against the Company, certain of its officers and directors (the Individual Defendants), and several investment banks that were underwriters of the Company s IPO. The cases were filed in the United States District Court for the Southern District of New York, purportedly on behalf of investors who purchased the Company s stock between August 10, 2000 and December 6, 2000. In addition, similar lawsuits were filed against approximately 300 other issuers and related parties. The purported class action alleges violations of Sections 11 and 15 of the Securities Act of 1933 and Sections 10(b), Rule 10b-5 and 20(a) of the Securities Exchange Act of 1934 against the Company and Individual Defendants. The plaintiffs have since dismissed the Individual Defendants without prejudice. The suits allege that the underwriter defendants agreed to allocate stock in the Company s IPO to certain investors in exchange for excessive and undisclosed commissions and agreements by those investors to make additional purchases in the aftermarket at pre-determined prices. The plaintiffs allege that the prospectus for the Company s IPO was false and misleading and in violation of the securities laws because it did not disclose these arrangements. The action seeks damages in an unspecified amount. On February 19, 2003, the Court dismissed the Section 10(b) claim against the Company, but denied the motion to dismiss the Section 11 claim.

EQUINIX, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In July 2003, a Special Litigation Committee of the Equinix Board of Directors approved a settlement agreement and related agreements which set forth the terms of a settlement between the Company, the Individual Defendants, the plaintiff class and the vast majority of the other approximately 300 issuer defendants and the individual defendants currently or formerly associated with those companies. Among other provisions, the settlement provides for a release of the Company and the Individual Defendants and the Company s agreeing to assign away, not assert, or release certain potential claims the Company may have against its underwriters. The settlement agreement also provides a guaranteed recovery of $1 billion to plaintiffs for the cases relating to all of the approximately 300 issuers. To the extent that the underwriter defendants settle all of the cases for at least $1 billion, no payment will be required under the issuers settlement agreement. To the extent that the underwriter defendants settle for less than $1 billion, the issuers are required to make up the difference. On April 20, 2006, JPMorgan Chase and the plaintiffs reached a preliminary agreement for a settlement for $425 million. The Court has not yet approved the JPMorgan Chase settlement. However, if it is finally approved, then the maximum amount that the issuers insurers will be potentially liable for is $575 million. It is anticipated that any potential financial obligation of Equinix to plaintiffs pursuant to the settlement, of which such claims are currently expected to be less than $3.4 million, will be covered by existing insurance and the Company does not expect that the settlement will involve any payment by the Company. However, if the JPMorgan Chase settlement is finally approved, the Company s maximum financial obligation to the plaintiffs pursuant to the settlement agreement would be less than $2 million. The Company has no information as to whether there are any material limitations on the expected recovery by other issuer defendants of any potential financial obligation to plaintiffs from their own insurance carriers. On February 15, 2005, the court granted preliminary approval of the settlement agreement, subject to certain modifications consistent with its opinion. Those modifications have been made. On March 20, 2006, the Underwriter Defendants submitted objections to the settlement to the Court. The Court held a hearing regarding these and other objections to the settlement at a fairness hearing on April 24, 2006, but has not yet issued a ruling. There is no assurance that the court will grant final approval to the settlement. As approval by the Court cannot be assured, the Company is unable at this time to determine whether the outcome of the litigation would have a material impact on its results of operations, financial condition or cash flows.

On October 13, 2004, the Court certified a Section 11 class in four of the six cases that were the subject of class certification motions and determined that the class period for Section 11 claims is the period between the IPO and the date that unregistered shares entered the market. The Court noted that its decision on those cases is intended to provide strong guidance to all parties regarding class certification in the remaining cases. The Underwriter Defendants sought leave to appeal the class certification decision and the Second Circuit has accepted the appeal. Plaintiffs have not yet moved to certify a class in the Equinix case. Until the settlement is finalized and approved by the Court, or in the event such settlement is not approved, the Company and its officers and directors intend to continue to defend the actions vigorously. While an unfavorable outcome to this case is reasonably possible, and the Company can estimate its potential exposure to be less than approximately $3.4 million, it is not probable. In addition, as noted above, any payments are expected to be covered by existing insurance and, as a result, the Company does not expect that the settlement will involve any payment by the Company. As a result, the Company has not accrued for any settlements in connection with this litigation as of September 30, 2006.

Estimated and Contingent Liabilities

The Company estimates exposure on certain liabilities, such as income and property taxes, based on the best information available at the time of determination. With respect to real and personal property taxes, the Company records what it can reasonably estimate based on prior payment history, current landlord estimates or estimates based on current or changing fixed asset values in each specific municipality, as applicable. However, there are circumstances beyond the Company s control whereby the underlying value of the property or basis for which the tax is calculated on the property may change, such as a landlord selling the underlying property of one of the Company s IBX center leases or a municipality changing the assessment value in a jurisdiction and, as a result, the Company s property tax obligations may vary from period to period. Based upon the most current facts and circumstances, the Company makes the necessary property tax accruals for each of its reporting periods. However, revisions in the Company s estimates of the potential or actual liability could materially impact the financial position, results of operations or cash flows of the Company.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In July 2005, the Company received a Notice of Proposed Assessment of Income Tax from the state of Hawaii asserting a tax deficiency, plus interest, totaling $613,000 (the Tax Assessment). The deficiency is stemmed from certain refundable tax credits that the state of Hawaii subsequently disallowed in the examination of the Hawaii income tax returns for the tax years of 2000 and 2001 filed by Pihana Pacific, Inc., which the Company acquired on December 31, 2002. On January 12, 2006 the Company filed a request with the Board of Review in the state of Hawaii to appeal the Tax Assessment. The Company strongly believes the disallowance of the refundable tax credits by the state of Hawaii is inconsistent with the applicable tax laws and that it has meritorious defenses to the claim. The Company does not believe it is probable it will be required to pay the Tax Assessment upon the completion of the appeals process. There has been no significant development with respect to the appeal request. The Company is still waiting for a response from the State of Hawaii regarding the scheduling of a meeting with the Board of Review. As a result, the Company has not accrued for any loss contingencies in connection with this Tax Assessment as of September 30, 2006.

From time to time, the Company may have certain contingent liabilities that arise in the ordinary course of its business activities. The Company accrues contingent liabilities when it is probable that future expenditures will be made and such expenditures can be reasonably estimated. In the opinion of management, there are no pending claims of which the outcome is expected to result in a material adverse effect in the financial position, results of operations or cash flows of the Company.

Operating Lease Amendments

In February 2006, the Company amended the lease to its corporate headquarter office in Foster City, California, to expand to the fourth floor of the building, which adds approximately 20,000 of additional square feet, and to extend the lease term an additional three years to March 2011.

Other Purchase Commitments

Primarily as a result of the Company s recent Washington, D.C. Metro Area IBX Expansion Project, Chicago Metro Area IBX Expansion Project and New York Metro Area IBX Expansion Project (see Note 2), as of September 30, 2006, the Company was contractually committed for $61,203,000 of unaccrued capital expenditures, primarily for IBX equipment not yet delivered and labor not yet provided, in connection with the work necessary to open these IBX centers and make them available to customers for installation. In addition, the Company has numerous other, non-capital purchase commitments in place as of September 30, 2006, such as commitments to purchase power in select locations, primarily in the U.S. and Singapore, through 2006 and 2007 and other open purchase orders which contractually bind the Company for goods or services to be delivered or provided during the remainder of 2006. Such other miscellaneous purchase commitments total $7,586,000 as of September 30, 2006.

13. Other Comprehensive Income and Loss

The components of other comprehensive income and loss are as follows (in thousands) (unaudited):

	Three months ended September 30,		Nine months ended September 30,	
	2006	**2005**	**2006**	**2005**
Net loss	$ (5,168)	$ (783)	$ (15,508)	$ (10,008)
Unrealized gain (loss) on available for sale securities	308	(168)	289	(426)
Foreign currency translation gain (loss)	(3)	(96)	1,376	(988)
Comprehensive loss	$ (4,863)	$ (1,047)	$ (13,843)	$ (11,422)

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

There were no significant tax effects on comprehensive loss for the three and nine months ended September 30, 2006 and 2005.

14. Segment Information

The Company and its subsidiaries are principally engaged in the design, build-out and operation of network neutral IBX centers. All revenues result from the operation of these IBX centers. The Company s chief operating decision-maker evaluates performance, makes operating decisions and allocates resources based on financial data consistent with the presentation in the accompanying consolidated financial statements.

The Company s geographic statement of operations disclosures are as follows (in thousands) (unaudited):

	Three months ended September 30,		Nine months ended September 30,	
	2006	2005	2006	2005
Total revenues:				
United States	$ 63,654	$ 50,527	$ 178,394	$ 137,927
Asia-Pacific	10,072	7,569	28,749	21,332
	$ 73,726	$ 58,096	$ 207,143	$ 159,259
Cost of revenues:				
United States	$ 43,529	$ 35,859	$ 121,507	$ 101,558
Asia-Pacific	5,608	5,096	16,538	15,081
	$ 49,137	$ 40,955	$ 138,045	$ 116,639
Income (loss) from operations:				
United States	$ (3,967)	$ 541	$ (9,619)	$ (3,944)
Asia-Pacific	896	(307)	524	(1,823)
	$ (3,071)	$ 234	$ (9,095)	$ (5,767)

The Company s long-lived assets are located in the following geographic areas (in thousands):

	September 30, 2006 (unaudited)	December 31, 2005
United States	$ 520,099	$ 457,280
Asia-Pacific	34,441	32,005
	$ 554,540	$ 489,285

The Company s goodwill totaling $22,710,000 and $21,654,000 as of September 30, 2006 and December 31, 2005, respectively, is part of the Company s Singapore reporting unit, which is reported within the Asia-Pacific geographic area.

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Revenue information on a services basis is as follows (in thousands) (unaudited):

	Three months ended September 30, 2006	Three months ended September 30, 2005	Nine months ended September 30, 2006	Nine months ended September 30, 2005
Colocation	$ 51,678	$ 40,138	$ 145,235	$ 109,479
Interconnection	13,862	10,527	38,310	29,696
Managed infrastructure	4,066	3,626	12,045	10,448
Rental	312		1,169	
Recurring revenues	69,918	54,291	196,759	149,623
Non-recurring revenues	3,808	3,805	10,384	9,636
	$ 73,726	$ 58,096	$ 207,143	$ 159,259

No single customer accounted for 10% of the Company s revenues for the three and nine months ended September 30, 2006. Revenue from one customer accounted for 11% of the Company s revenues for both the three and nine months ended September 30, 2005. No other single customer accounted for more than 10% of the Company s revenues for the three and nine months ended September 30, 2005. Accounts receivables from the customer mentioned above accounted for 10% and 12% of the Company s gross accounts receivables as of September 30, 2006 and 2005, respectively. No other single customer accounted for more than 10% of the Company s gross accounts receivables as of September 30, 2006 and 2005.

15. Restructuring Charges

2004 Restructuring Charges

In December 2004, in light of the availability of fully built-out data centers in select markets at costs significantly below those costs the Company would incur in building out new space, the Company made the decision to exit leases for excess space adjacent to one of the Company s New York metro area IBXs, as well as space on the floor above its original Los Angeles IBX. As a result of the Company s decision to exit these spaces, the Company recorded restructuring charges totaling $17,685,000, which represents the present value of the Company s estimated future cash payments, net of any estimated subrental income and expense, through the remainder of these lease terms, as well as the write-off of all remaining property and equipment attributed to the partial build-out of the excess space on the floor above its Los Angeles IBX as outlined below. Both lease terms run through 2015.

The Company adopted SFAS No. 146, Accounting for Costs Associated with Exit or Disposal Activities , at the beginning of its fiscal year 2003. Under the provisions of SFAS No. 146, the Company estimated the future cash payments required to exit these two leased spaces, net of any estimated subrental income and expense, through the remainder of these lease terms and then calculated the present value of such future cash flows in order to determine the appropriate restructuring charge to record. The Company records accretion expense to accrete its accrued restructuring liability up to an amount equal to the total estimated future cash payments necessary to complete the exit of these leases. Should the actual lease exit costs differ from the Company s estimates, the Company may need to adjust its restructuring charges associated with the excess lease spaces, which would impact net income in the period such determination was made.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

A summary of the movement in the 2004 accrued restructuring charge from December 31, 2005 to September 30, 2006 is outlined as follows (in thousands) (unaudited):

	Accrued restructuring charge as of December 31, 2005	Accretion expense	Restructuring charge	Cash payments	Accrued restructuring charge as of September 30, 2006
Estimated lease exit costs	$ 13,702	$ 605	$ 1,527	$ (1,367)	$ 14,467
	13,702	$ 605	$ 1,527	$ (1,367)	14,467
Less current portion	(2,171)				(3,464)
	$ 11,531				$ 11,003

During the three months ended September 30, 2006, the Company recorded an additional restructuring charge of $1,527,000 as a result of revised sublease assumptions on these two excess space leases as new information became available. As the Company currently has no plans to enter into lump sum lease terminations with either of the landlords associated with these two excess space leases, the Company has reflected its accrued restructuring liability as both current and non-current on the accompanying balance sheets as of September 30, 2006 and December 31, 2005. The Company is contractually committed to these two excess space leases through 2015.

2005 Restructuring Charges

In October 2005, in light of the availability of fully or partially built-out data centers in the Silicon Valley, including the possibility of expansion among some of the four IBX centers the Company currently has in the Silicon Valley, the Company made the decision that retaining the approximately 40 acre San Jose Ground Lease for future expansion was no longer economical. In conjunction with this decision, the Company entered into an agreement with the landlord of this property for the early termination of the San Jose Ground Lease property whereby the Company will pay $40,000,000 over the next four years plus property taxes, commencing January 1, 2006, to terminate this lease, which would otherwise require significantly higher cumulative lease payments through 2020 (the San Jose Ground Lease Termination). As a result of the San Jose Ground Lease Termination, the Company recorded a $33,814,000 restructuring charge in the fourth quarter of 2005, which represents the present value of the Company s estimated future cash payments to exit this property, as well as the write-off of all remaining property and equipment attributed to the development of this property.

The Company estimated the future cash payments required to exit the San Jose Ground Lease, net of any estimated subrental income and expense, through the remainder of these lease terms and then calculated the present value of such future cash flows in order to determine the appropriate restructuring charge to record. The Company s use of this property terminates on December 31, 2007 and can be terminated at any time prior to December 31, 2007 upon the landlord providing the Company at least ten days prior written notice; however, even if the landlord early terminates, the Company is still required to pay the full $40,000,000 of payments due. The Company records accretion expense to accrete its accrued restructuring liability up to an amount equal to the total estimated future cash payments necessary to complete the exit of the San Jose Ground Lease.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

A summary of the movement in the 2005 accrued restructuring charge from December 31, 2005 to September 30, 2006 is outlined as follows (in thousands) (unaudited):

	Accrued restructuring charge as of December 31, 2005	Accretion expense	Cash payments	Accrued restructuring charge as of September 30, 2006
Estimated lease exit costs	$ 36,129	$ 1,796	$ (7,846)	$ 30,079
	36,129	$ 1,796	$ (7,846)	30,079
Less current portion	(10,229)			(10,384)
	$ 25,900			$ 19,695

16. Recent Accounting Pronouncements

In October 2005, the FASB issued FASB Staff Position No. SFAS 13-1 (FSP SFAS 13-1), which addresses the accounting for rental costs associated with building and ground operating leases that are incurred during a construction period. The FASB decided that such rental costs incurred during a construction period shall be recognized as rental expense. A lessee should cease capitalizing rental costs as of the effective date of FSP SFAS 13-1. The guidance in FSP SFAS 13-1 shall be applied to the first reporting period beginning after December 15, 2005. Early adoption is permitted for financial statements or interim financial statements that have not yet been issued. A lessee shall cease capitalizing rental costs as of the effective date of FSP SFAS 13-1 for operating lease arrangements entered into prior to the effective date of FSP SFAS 13-1. The adoption of FSP SFAS 13-1 has not had a significant impact on the Company s financial position, results of operations or cash flows as the Company s accounting policy for such rental costs has always been to expense such costs.

In November 2005, the FASB issued FASB Staff Position No. SFAS 115-1 and SFAS 124-1 (FSP SFAS 115-1 and 124-1), which addresses the determination as to when an investment is considered impaired, whether that impairment is other than temporary, and the measurement of an impairment loss. FSP SFAS 115-1 and 124-1 also includes accounting considerations subsequent to the recognition of an other-than-temporary impairment and requires certain disclosures about unrealized losses that have not been recognized as other-than-temporary impairments. The guidance in FSP SFAS 115-1 and 124-1 amends FASB Statements No. 115, Accounting for Certain Investments in Debt and Equity Securities, and No. 124, Accounting for Certain Investments Held by Not-for-Profit Organizations, and APB Opinion No. 18, The Equity Method of Accounting for Investments in Common Stock. The guidance in FSP SFAS 115-1 and 124-1 shall be applied to the first reporting period beginning after December 15, 2005. The adoption of FSP SFAS 115-1 and 124-1 has not had a significant impact on the Company s financial position, results of operations and cash flows.

In February 2006, the FASB issued SFAS No. 155, Accounting for Certain Hybrid Instruments, an amendment of SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities and SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities-a replacement of FASB Statement No. 125 (SFAS No. 155). SFAS No. 155 improves the financial reporting of certain hybrid financial instruments by requiring more consistent accounting that eliminates exemptions and provides a means to simplify the accounting for such instruments. Specifically, SFAS No. 155 allows financial instruments that have embedded derivatives to be accounted for as a whole (eliminating the need to bifurcate the derivative from its host) if the holder elects to account for the whole instrument on a fair value basis. SFAS No. 155 also (i) clarifies which interest-only strips and principal-only strips are not subject to the requirements of SFAS No. 133; (ii) establishes a requirement to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation; (iii) clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives and (iv) amends SFAS No. 140 to

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

eliminate the prohibition on a qualifying special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument. SFAS No. 155 is effective for all financial instruments acquired or issued after the beginning of an entity s first fiscal year that begins after September 15, 2006. The Company is currently in the process of evaluating the impact that the adoption of SFAS No. 155 will have on its financial position, results of operations and cash flows.

In April 2006, the FASB issued FASB Staff Position No. FIN 46(R)-6 (FSP FIN 46(R)-6), which addresses how a reporting enterprise should determine the variability to be considered in applying FASB Interpretation No. 46, Consolidation of Variable Interest Entities , as amended (FIN 46(R)). The variability that is considered in applying FIN 46(R) affects the determination of (a) whether the entity is a variable interest entity, (b) which interests are variable interests in the entity and (c) which party, if any, is the primary beneficiary of the variable interest entity. That variability will affect any calculation of expected losses and expected residual returns, if such a calculation is necessary. FSP FIN 46(R)-6 provides additional guidance to consider for determining variability. FSP FIN 46(R)-6 is effective beginning the first day of the first reporting period beginning after June 15, 2006. The adoption of FSP FIN 46(R)-6 has not had a significant impact on the Company s financial position and results of operations.

In June 2006, the FASB approved EITF Issue No. 06-3, How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That is, Gross versus Net Presentation) (EITF 06-3). EITF 06-3 includes any tax assessed by a governmental authority that is directly imposed on a revenue-producing transaction between a seller and a customer and may include, but is not limited to, sales, use, value added and some excise taxes. EITF 06-3 concludes that the presentation of taxes on either a gross (included in revenue and costs) or a net (excluded from revenue) basis is an accounting policy decision that should be disclosed. In addition, for any such taxes that are reported on a gross basis, an entity should disclose the amounts of those taxes in interim and annual financial statements for each period for which an income statement is presented if those amounts are significant. The provisions of EITF 06-3 should be applied to financial reports for interim and annual reporting periods beginning after December 15, 2006, with earlier adoption permitted. The Company believes that the adoption of EITF 06-3 will not have any significant impact on the Company s financial position and results of operations.

In July 2006, the FASB issued Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48), which clarifies the accounting for uncertainty in income taxes recognized in the financial statements in accordance with FASB Statement No. 109, Accounting for Income Taxes. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is currently in the process of evaluating the impact that the adoption of FIN 48 will have on its financial position, results of operations and cash flows.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements (SFAS No. 157). SFAS No. 157 defines fair value, establishes a framework for measuring fair value under GAAP, and expands disclosures about fair value measurements. SFAS No. 155 is effective for fiscal years beginning after December 15, 2007. The Company is currently in the process of evaluating the impact that the adoption of SFAS No. 157 will have on its financial position, results of operations and cash flows.

In September 2006, the SEC issued Staff Accounting Bulletin No. 108, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements (SAB 108), to address diversity in practice in quantifying financial statement misstatements. SAB 108 requires that the Company quantifies misstatements based on their impact on each of its financial statements and related disclosures. The Company will adopt the provisions of SAB 108 during the fourth quarter of 2006. The Company is currently in the process of evaluating the impact that the adoption of SAB 108 will have on its financial position, results of operations and cash flows.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

17. Subsequent Events

In October 2006, the Company utilized an additional $7,800,000 under the letters of credit sublimit associated with the Silicon Valley Bank Credit Line Amendment in connection with the new lease for the New York metro area IBX expansion project and also fully repaid the $40,000,000 Borrowing from the Silicon Valley Bank Credit Line Amendment (see Note 9).

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Item 2.

MANAGEMENT S DISCUSSION AND ANALYSIS

OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The information in this discussion contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Such statements are based upon current expectations that involve risks and uncertainties. Any statements contained herein that are not statements of historical fact may be deemed to be forward-looking statements. For example, the words believes, anticipates, plans, expects, intends and similar expressions are intended to identify forward-looking statements. Our actual results and the timing of certain events may differ significantly from the results discussed in the forward-looking statements. Factors that might cause such a discrepancy include, but are not limited to, those discussed in Liquidity and Capital Resources below and Risk Factors in Item 1A of Part II of this Quarterly Report on Form 10-Q. All forward-looking statements in this document are based on information available to us as of the date of this Report and we assume no obligation to update any such forward-looking statements.

Overview

Equinix provides network neutral colocation, interconnection and managed services to enterprises, content companies, systems integrators and the world s largest network providers. Through our IBX centers in eleven markets in the U.S. and Asia-Pacific, customers can directly interconnect with each other for critical traffic exchange requirements. As of September 30, 2006, we operate IBX centers in the Chicago, Dallas, Honolulu, Los Angeles, New York, Silicon Valley and Washington, D.C. metro areas in the United States and Hong Kong, Singapore, Sydney and Tokyo in the Asia-Pacific region.

Direct interconnection to our aggregation of networks, which serve more than 90% of the world s Internet routes, allows our customers to increase performance while significantly reducing costs. Based on our network neutral model and the quality of our IBX centers, we believe we have established a critical mass of customers. As more customers locate in our IBX centers, it benefits their suppliers and business partners to do so as well to gain the full economic and performance benefits of direct interconnection. These partners, in turn, pull in their business partners, creating a network effect of customer adoption. Our interconnection services enable scalable, reliable and cost-effective interconnection and traffic exchange thus lowering overall cost and increasing flexibility. Our focused business model is based on our critical mass of customers and the resulting network effect. This critical mass and the resulting network effect, combined with our strong financial position, continue to drive new customer growth and bookings.

Historically, our market has been served by large telecommunications carriers who have bundled their telecommunications products and services with their colocation offerings. A number of these telecommunications carriers have eliminated or reduced their colocation footprint to focus on their core businesses. In 2003, as an example, one major telecommunications company, Sprint, announced its plans to exit the colocation and hosting market in order to focus on its core service offerings, while another telecommunications company, Cable & Wireless Plc, sold its U.S. assets to another telecommunications company, Savvis Communications Corp, in a bankruptcy auction. In 2005 and 2006, other providers, such as Abovenet and Verio, have selectively sold off certain of their colocation centers. Each of these colocation providers own and operate a network. We do not own or operate a network, yet have greater than 200 networks operating out of our IBX centers. As a result, we are able to offer our customers a substantial choice of networks given our network neutrality thereby allowing our customers to choose from numerous network service providers. We believe this is a distinct and sustainable competitive advantage, especially when the telecommunications industry is experiencing many business challenges and changes as evidenced by the numerous bankruptcies and consolidations within this industry during the past several years. Furthermore, this industry consolidation has constrained the supply of suitable data center space and has had a positive effect on industry pricing.

Our utilization rate represents the percentage of our cabinet space billing versus total cabinet space available. Our utilization rate grew to 54% as of September 30, 2006 from 51% as of September 30, 2005; however, although we have substantial capacity for growth, our utilization rates vary from market to market among our IBX centers in the eleven markets across the U.S. and Asia-Pacific. We continue to monitor the

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available capacity in each of our selected markets. To the extent we have limited capacity available in a given market, it may limit our ability for growth in that market. Once capacity becomes limited, we will perform demand studies to determine if future expansion is warranted. In addition, power and cooling requirements for some customers are growing on a per unit basis. As a result, customers are consuming an increasing amount of power per cabinet. Although we generally do not control the amount of draw our customers take from installed circuits, we have negotiated power consumption limitations with certain of our high power demand customers. We could face power limitations in our centers even though we may have additional physical capacity available within a specific IBX center. This could have a negative impact on the available utilization capacity of a given center, which could have a negative impact on our ability to grow revenues, affecting our financial performance, operating results and cash flows. As a result of these power limitations in our existing IBX centers, the maximum utilization rate that we expect to achieve for most IBX centers until we consider an IBX center full or sold-out is approximately 75-80% depending on the building configurations.

Strategically, we will continue to look at attractive opportunities to grow our market share and selectively improve our footprint and service offerings, such as our acquisition of the Sprint property in Santa Clara in December 2003, our 2004 expansions in the Washington, D.C. and Silicon Valley metro area markets, our 2005 expansions in the Silicon Valley, Chicago and Los Angeles metro area markets and our 2006 expansions in the Washington, D.C., Chicago and New York metro area markets, which are expected to open in 2007 (see Recent Developments below). However, we will continue to be very selective with any similar opportunity. As was the case with these recent expansions in the Washington, D.C., Silicon Valley, Chicago and Los Angeles area markets, our expansion criteria will be dependent on demand from new and existing customers, quality of the design, power capacity, access to networks, capacity availability in current market location, amount of incremental investment required by us in the targeted property, lead-time to break-even and in-place customers. Like our recent expansions, the right combination of these factors may be attractive to us. Dependent on the particular deal, these acquisitions may require upfront cash payments and additional capital expenditures or may be funded through long-term financing arrangements in order to bring these centers up to Equinix standards. Property expansion may be in the form of a purchase of real property, as was the case with our recent Washington, D.C. and Chicago metro area property acquisitions, or a long-term leasing arrangement.

In addition to our successful strategy of acquiring previously or partially built-out centers, we are currently starting new construction to build out new IBX centers in the Washington, D.C, Chicago and New York metro areas. As part of our strategy, we will continue to contemplate the possibility of new construction in selective markets where the inventory for high quality data centers is limited. Decisions to build will consider factors such as customer demand, market pricing and the financial returns associated with the construction. Future purchases or construction may be completed by us or with partners or potential customers to minimize the outlay of cash, which can be significant.

Recent Developments

In January 2006, the Compensation Committee of the Board of Directors approved stock options to be granted to employees, excluding executive officers, to purchase an aggregate of 648,500 shares of common stock as part of our annual refresh program. In addition, the Compensation Committee of the Board of Directors also approved the issuance of 250,000 restricted shares of common stock to executive officers. The restricted shares are subject to four-year vesting, and will only vest at certain time intervals and if the stock appreciates to pre-determined levels. All such equity awards were accounted for under the provisions of SFAS No. 123(R), Share-Based Payment, and related pronouncements, which had a significant impact on us. We expect stock-based compensation expense related to these equity awards to impact our results of operations through 2011. For further information on stock-based compensation, refer to Accounting for Stock-Based Compensation in Critical Accounting Policies and Estimates below.

In February 2006, we announced our intention to build out a new IBX center within our Ashburn campus in order to further expand our existing Washington, D.C. metro area IBX center. In May 2006, we began new construction to build out one of the undeveloped buildings located on our Ashburn campus for a cost of approximately $60.0 million, of which approximately $56.0 million is expected to be incurred in 2006. The center will feature an updated design that will enable us to support the increased power and cooling demands of customers. We intend to open the new center for customers during the three months ending

March 31, 2007. We refer to this project as the Washington, D.C. metro area IBX expansion project. The Washington, D.C. metro area IBX expansion project will fulfill our obligation to invest at least $40.0 million in capital improvements to our Ashburn campus by December 31, 2007 pursuant to the terms of the Ashburn campus mortgage payable. In September 2006, we received loan commitments, subject to customary closing conditions, for $40.0 million to finance this Washington, D.C. metro area IBX expansion project in a long-term financing arrangement at anticipated rates of approximately 8%, which we expect to close during the fourth quarter of 2006. In September 2006, we elected to borrow $40.0 million from the $75.0 million Silicon Valley Bank revolving credit line to partially finance this project.

In June 2006, we purchased a 228,000 square foot stand-alone office/warehouse complex for $9.8 million, including closing costs, which we paid for in full during June 2006. We intend to build an IBX center, which will be our second IBX center location in the Chicago metro area, in multiple phases. We refer to this project as the Chicago metro area IBX expansion project. This new IBX center will be interconnected to our existing downtown Chicago IBX centers through redundant dark fiber links managed by us. We plan to invest approximately $165.0 million to build out the first phase, of which approximately $40.0 million is expected to be incurred in 2006. This includes an investment of approximately $40.0 million to construct a specially built 250,000 square foot shell, acquire access to power and provision fiber for interconnection to our downtown Chicago IBX center location. The site development plan allows a second expansion phase at an incremental investment of $30.0 million. We intend to open the new center for customers during the three months ended September 30, 2007. In September 2006, we received loan commitments, subject to customary closing conditions, for $110.0 million to finance at least 60% of the build costs or a maximum of $110.0 million in a long-term financing arrangement at anticipated rates of approximately 8%, which we expect to close during the fourth quarter of 2006. In September 2006, we elected to borrow $40.0 from the $75.0 million Silicon Valley Bank revolving credit line to partially finance this project.

In June 2006, the Audit Committee of the Board of Directors commenced an independent investigation of our historical stock option granting practices and related accounting with the assistance of independent outside legal counsel. This review covers the timing and pricing of all stock option grants made under our stock option plans since August 11, 2000, the day after our Initial Public Offering (IPO). As previously announced on June 12, 2006, we are currently cooperating with the Securities and Exchange Commission (SEC) regarding the SEC s informal inquiry requesting documents related to our stock option grants and practices. We also announced on June 29, 2006 that we received a grand jury subpoena from the U.S. Attorney for the Northern District of California (US Attorney) and are cooperating fully with the U.S. Attorney s Office in connection with this subpoena. The subpoena requests documents relating to our stock option grants and practices. Based on the results of its review, the Audit Committee of the Board of Directors determined that the accounting measurement dates of certain stock option grants issued in the past differ from the actual grant dates. The Audit Committee of the Board of Directors concluded that we did not engage in intentional or fraudulent misconduct in the granting of stock options. However, the accounting measurement dates for certain historical stock option grants differed from their actual grant dates. As a result of revising the accounting measurement dates for these stock option grants, we have recorded an additional non-cash stock-based compensation charge totaling $444,000 in our consolidated financial statements for nine months ended September 30, 2006. The amount of the charge was computed pursuant to the requirements of APB 25 for all historical periods through December 31, 2005 and pursuant to SFAS 123(R) for the three month period ended March 31, 2006. This $444,000 stock-based compensation charge represents the total charge for historical periods that we need to record as a result of the Audit Committee s conclusion on this matter. This compensation charge has no effect on our current cash position. We concluded that the cumulative charge as a result of the difference between the measurement dates used for financial accounting and reporting purposes and the actual grant dates for certain stock option grants, totaling $444,000, was not material to any previously-reported historical period nor is it expected to be material to the current fiscal year. As such, this cumulative charge totaling $444,000 was recorded in the statement of operations for the nine months ended September 30, 2006, versus restating prior periods.

In June 2006, we received an informal inquiry from the SEC and a grand jury subpoena from the U.S. Attorney requesting documents relating to our stock option grants and practices. Such inquiries are believed to be related to recent widespread investigations into the practices of public companies relating to the timing of option grants. We intend to fully cooperate in all government investigations.

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On June 29, 2006 and September 18, 2006, shareholder derivative complaints were filed in the Superior Court of the State of California, County of San Mateo against certain of our current and former officers and directors (the Defendants). The complaints allege that the Defendants breached their fiduciary duties by engaging in allegedly improper stock option grant practices since at least 2000, and by failing to adequately disclose such transactions. The complaints seek unspecified monetary damages, corporate governance changes and restitution. On October 13, 2006, a third shareholder derivative complaint related to allegedly improper stock option grant practices was filed in the United States District Court for the Northern District of California against certain of our current and former officers and directors. The complaint seeks unspecified monetary and punitive damages, corporate governance changes, and the imposition of a constructive trust over certain stock options and related proceeds. At the appropriate time, we expect to file motions to dismiss these lawsuits due to the plaintiffs unexcused failure to make a demand on us before filing the actions. In addition to the current derivative claims, we may be subject to additional derivative or other lawsuits that may be presented on an individual or class basis alleging claims based on our stock option granting practices. Similar lawsuits and investigations have been commenced against numerous other companies based on similar allegations.

In August 2006, we amended the $50.0 million Silicon Valley Bank revolving credit line to increase the line to $75.0 million and added General Electric Capital Corporation (GE) as a lender. We refer to this transaction as the $75.0 million Silicon Valley Bank revolving credit line. The $75.0 million Silicon Valley Bank revolving credit line allows for issuance of letters of credit (in addition to revolving borrowings). The $75.0 million Silicon Valley Bank revolving credit line also has an option for us to increase the amount of the line to $100.0 million at a later date, subject to approval of the lender or lenders electing to participate in such increase. Borrowings under the $75.0 million Silicon Valley Bank revolving credit line will continue to bear interest at variable interest rates, plus the applicable margins which were in effect prior to the amendment, based on either prime rates or LIBOR rates. The $75.0 million Silicon Valley Bank revolving credit line matures on September 15, 2008 and is secured by substantially all of our domestic personal property assets and certain of our real property leases and contains several financial covenants, which require compliance with maximum leverage and working capital ratios and a minimum EBITDA target. In September 2006, we borrowed $40.0 million from the $75.0 million Silicon Valley Bank revolving credit line. In October 2006, we utilized an additional $7.8 million under the letters of credit sublimit associated with the $75.0 million Silicon Valley Bank revolving credit line in connection with the new lease for the New York metro area IBX expansion project and we fully repaid the $40.0 million borrowing from the $75.0 million Silicon Valley Bank revolving credit line. See Debt Obligations Non-Convertible Debt below for further discussion.

In September 2006, we entered into a long-term lease for an approximately 340,000 square foot building in the New York metro area. We intend to build an IBX center, which will be our fourth IBX center in the New York metro area, and this new center will be interconnected to our existing IBX centers in the New York metro area through redundant dark fiber links managed by us. We refer to this project as the New York metro area IBX expansion project. Payments under this lease total $59.4 million, which will be paid in monthly installments and payable through September 2021. The lease, which commenced in October 2006, contains a three-year option to purchase the building for $39.0 million. We intend to build out the new center in multiple phases and expect to open the first phase for customers during the three months ended September 30, 2007. As previously announced, we intend to invest approximately $80.0 million to $90.0 million to build out the first phase of the new center, of which $4.0 million is expected to be incurred in 2006. We expect to finance at least 60% of the capital expenditures required to complete the New York metro area IBX expansion project in the form of short and long-term financing arrangements, which we expect to obtain in 2007.

Critical Accounting Policies and Estimates

Equinix s financial statements and accompanying notes are prepared in accordance with generally accepted accounting principles in the United States of America. Preparing financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, sales and expenses. These estimates and assumptions are affected by management s application of accounting policies. Critical accounting policies for Equinix include revenue recognition and allowance for doubtful accounts, accounting for income taxes, estimated and contingent liabilities, accounting for property and equipment, impairment of long-lived assets, accounting for asset retirement obligations, accounting for leases and IBX acquisitions, accounting for restructuring charges and accounting for stock-based compensation, which are discussed in more detail under the caption Critical Accounting Policies and

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Estimates in our 2005 Annual Report on Form 10-K. As a result of our adoption of SFAS No. 123(R), Share-Based Payment, and related pronouncements, during the three months ended March 31, 2006, we have updated accounting for stock-based compensation as discussed below.

Accounting for Stock-Based Compensation

We adopted the provisions of, and account for stock-based compensation in accordance with, SFAS No. 123(R), Share-Based Payment, and related pronouncements (SFAS 123(R)), during the three months ended March 31, 2006. As a result of our adoption of SFAS 123(R), we recorded stock-based compensation expense of $6.9 million and $23.5 million for the three and nine months ended September 30, 2006, respectively. For the three and nine months ended September 30, 2005, we recorded stock-based compensation expense in accordance with APB 25 of $1.4 million and $6.3 million, respectively. The fair value of stock options and employee stock purchase plan shares were valued using the Black-Scholes option-pricing model while the fair value of our restricted stock grants were valued using a Monte Carlo simulation option-pricing model. The determination of the fair value of stock-based payment awards on the date of grant using an option-pricing model is affected by our stock price as well as assumptions regarding a number of complex and highly subjective variables. These variables include our expected stock price volatility over the term of the awards, actual and projected employee stock option exercise behaviors or expected term, risk-free interest rate and expected dividends.

We record stock-based compensation expense on stock awards expected to vest during the period net of estimated forfeitures. The estimated forfeitures on unvested stock awards are assessed based on our historical stock awards activity and our expectations about future employee turnover, and these rates are subject to revision in subsequent periods if actual forfeitures differ from those estimates. Higher forfeitures will result in lower stock-based compensation expense while lower forfeiture rates will result in higher stock-based compensation expense. We estimate the expected volatility by using the average historical volatility of our common stock that we believe is the best representative of the future volatility. The expected term of options used is calculated by taking the average of the vesting term and the contractual term of the option, as illustrated in SAB 107. The risk-free interest rate used is based on U.S. Treasury zero-coupon issues with remaining terms similar to the expected term on our equity awards. We do not anticipate paying any cash dividends in the foreseeable future and, therefore, the expected dividend rate used is zero.

During the nine months ended September 30, 2006, stock options granted to employees had a total fair value of $34.7 million. Changes in assumptions (as well as different option-pricing models used for estimating the fair value of stock awards) can significantly affect our future period expense. Based on our analysis, the table below presents the possible impact of increases or decreases of individual variables (representing increases/decreases of 10%, 20%, 30% and 40%) in the assumptions to the fair value of employee stock options granted during the nine months ended September 30, 2006 (dollars in thousands):

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Expected volatility			Risk-free interest rate			Expected life		
Weighted average rate	**Increase/ decrease in fair value (%)**	**(1) Increase/ decrease in total expense**	**Weighted average rate**	**Increase/ decrease in fair value (%)**	**(1) Increase/ decrease in total expense**	**Weighted average life**	**Increase/ decrease in fair value (%)**	**(1) Increase/ decrease in total expense**
70%**(2)**			4.72%**(2)**			4.56**(2)**		
77%	6.59%	$ 2,290	5.19%	0.78%	$ 273	5.02	4.02%	$ 1,396
84%	12.80%	4,448	5.67%	1.56%	543	5.47	7.73%	2,684
91%	18.62%	6,469	6.14%	2.34%	812	5.93	11.16%	3,879
98%	24.04%	8,351	6.61%	3.11%	1,080	6.38	14.36%	4,989
63%	-6.95%	(2,415)	4.25%	-0.79%	(274)	4.10	-4.37%	(1,517)
56%	-14.24%	(4,947)	3.78%	-1.58%	(550)	3.65	-9.14%	(3,174)
49%	-21.83%	(7,583)	3.31%	-2.38%	(828)	3.19	-14.38%	(4,996)
42%	-29.66%	(10,306)	2.83%	-3.19%	(1,107)	2.74	-20.19%	(7,015)

(1) Increase/decrease in total expense is calculated based on percentage increase/decrease in fair value to the total fair value of $34.7 million of our employee stock options granted during the nine months ended September 30, 2006.

(2) Variables used in calculating the fair value of our employee stock options granted during the nine months ended September 30, 2006.

The table above shows that changes in expected volatility present the most significant impact to the increases/decreases of stock-based compensation expense compared to changes in other variables. Had the expected volatility increased by 40%, our stock-based compensation expense recognized, net of estimated forfeitures, for the nine months ended September 30, 2006 would have been approximately $696,000 higher than the reported stock-based compensation expense. Had the expected volatility decreased by 40%, our stock-based compensation expense recognized, net of estimated forfeitures, for the nine months ended September 30, 2006 would have been approximately $858,000 lower than the reported stock-based compensation expense. The assumptions used in calculating the fair value of stock-based awards represent our best estimates, but these estimates involve inherent uncertainties and the application of management judgment.

The guidance in SFAS 123(R) and SAB 107 is relatively new. The application of these principles may be subject to further interpretation and refinement over time. There are significant differences among valuation models, and there is a possibility that we will adopt different valuation models in the future. This may result in a lack of consistency in future periods and materially affect the fair value estimate of stock-based payments. It may also result in a lack of comparability with other companies that use different models, methods and assumptions.

As of September 30, 2006, the total stock-based compensation cost related to unvested equity awards not yet recognized, net of estimated forfeitures, totaled $48.3 million, which is expected to be recognized over a weighted-average period of 2.6 years.

Also see Note 10 of our Notes to Condensed Consolidated Financial Statements in Item 1 of this Quarterly Report on Form 10-Q.

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Results of Operations

Three Months Ended September 30, 2006 and 2005

Revenues. Our revenues for the three months ended September 30, 2006 and 2005 were split between the following revenue classifications (dollars in thousands):

	Three months ended September 30,			
	2006	%	2005	%
Recurring revenues	$ 69,918	95%	$ 54,291	93%
Non-recurring revenues:				
Installation and professional services	3,808	5%	2,946	6%
Other		0%	859	1%
	3,808	5%	3,805	7%
Total revenues	$ 73,726	100%	$ 58,096	100%

Our revenues for the three months ended September 30, 2006 and 2005 were geographically comprised of the following (dollars in thousands):

	Three months ended September 30,			
	2006	%	2005	%
U.S. revenues	$ 63,654	86%	$ 50,527	87%
Asia-Pacific revenues	10,072	14%	7,569	13%
Total revenues	$ 73,726	100%	$ 58,096	100%

We recognized revenues of $73.7 million for the three months ended September 30, 2006 as compared to revenues of $58.1 million for the three months ended September 30, 2005, a 27% increase. We analyze our business geographically between the U.S. and Asia-Pacific as further discussed below.

Our business is based on a recurring revenue model comprised of colocation, interconnection and managed infrastructure services. We consider these services recurring as our customers are billed on a fixed and recurring basis each month for the duration of their contract, which is generally one to three years in length. Our recurring revenues are a significant component of our total revenues comprising greater than 90% of our total revenues for the three months ended September 30, 2006 and 2005. Historically, approximately half of our then existing customers order new services in any given quarter representing greater than half of the new orders received in each quarter.

Our non-recurring revenues are primarily comprised of installation services related to a customer s initial deployment and professional services that we perform. These services are considered to be non-recurring as they are billed typically once and only upon completion of the installation or professional services work performed. These non-recurring revenues are typically billed on the first invoice distributed to the customer. Non-recurring installation fees, although generally paid in a lump sum upon installation, are deferred and recognized ratably over the longer of the term of the related contract or expected customer relationship. As a percent of total revenues, we expect non-recurring revenues to represent less than 10% of total revenues for the foreseeable future. Other non-recurring revenues are comprised primarily of customer settlements, which represent fees paid to us by customers who wish to terminate their contracts with us prior to their expiration.

In addition to reviewing recurring versus non-recurring revenues, we look at two other primary metrics when we analyze our revenues: 1) customer count and 2) utilization. Our customer count increased to 1,260 as of September 30, 2006 versus 1,093 as of September 30, 2005, an increase of 15%. Our utilization rate represents the percentage of our cabinet space billing versus total cabinet space available. Our utilization rate grew to 54% as of September 30, 2006 from 51% as of September 30, 2005; however, excluding the impact of our recent IBX center openings in the Chicago, Los Angeles and Silicon Valley

metro areas, our utilization rate would have been 63% as of September 30, 2006. Although we have substantial capacity for growth, our utilization rates vary from market to market among our IBX centers in the eleven markets across the U.S. and Asia-Pacific. We continue to monitor the available capacity in each of our selected markets. To the extent we have limited capacity available in a given market, it may limit our ability for growth in that market. Once capacity becomes limited, we perform demand studies to determine if future expansion is warranted. In addition, power and cooling requirements for some customers are growing on a per unit basis. As a result, customers are consuming an increasing amount of power per cabinet. Although we generally do not control the amount of draw our customers take from installed circuits, we have negotiated power consumption limitations with certain of our high power demand customers. We could face power limitations in our centers even though we may have additional physical capacity available within a specific IBX center. This could have a negative impact on the available utilization capacity of a given center, which could have a negative impact on our ability to grow revenues, affecting our financial performance, operating results and cash flows. As a result of these power limitations in our existing IBX centers, the maximum utilization rate that we expect to achieve for most IBX centers until we consider an IBX center full or sold-out is approximately 75-80% depending on the building configurations. Therefore, consistent with our recent expansion efforts in the Chicago, Los Angeles, Silicon Valley and Washington, D.C. metro area markets, we will continue to closely manage available space and power capacity in each of our operating markets and expect to continue to make strategic and selective expansions to our global footprint when and where appropriate.

U.S. Revenues. We recognized U.S. revenues of $63.6 million for the three months ended September 30, 2006 as compared to $50.5 million for the three months ended September 30, 2005, a 26% increase. U.S. revenues consisted of recurring revenues of $60.3 million and $47.2 million, respectively, for the three months ended September 30, 2006 and 2005, a 28% increase. U.S. recurring revenues consist primarily of colocation and interconnection services plus a nominal amount of managed infrastructure services and, commencing in the fourth quarter of 2005, in connection with our October 2005 purchase of the Ashburn campus property, a nominal amount of recurring rental income from the other tenants located on this property that we now own, which totaled $312,000 for the three months ended September 30, 2006. The period over period growth in recurring revenues was primarily the result of an increase in orders from both our existing customers and new customers acquired during the period as reflected in the growth in our customer count and utilization rate as discussed above, and selective price increases in each of our IBX markets. Total increase in revenues as a result of selective price increases for three months ended September 30, 2006 over the same period last year was approximately $532,000. In addition, we recorded $2.2 million of revenues from our new IBX centers in the Chicago, Los Angeles and Silicon Valley metro areas, which opened for business during the nine months ended September 30, 2006. We expect our U.S. recurring revenues, particularly colocation and interconnection services, to continue to remain our most significant source of revenue for the foreseeable future.

In addition, U.S. revenues consisted of non-recurring revenues of $3.3 million for both the three months ended September 30, 2006 and 2005. U.S. non-recurring revenues included $817,000 of contract settlement revenue for the three months ended September 30, 2005. Non-recurring revenues are primarily related to the recognized portion of deferred installation and professional services. U.S. non-recurring revenues, consisting of the recognized portion of deferred installation and professional services.

Asia-Pacific Revenues. We recognized Asia-Pacific revenues of $10.1 million for the three months ended September 30, 2006 as compared to $7.6 million for the three months ended September 30, 2005, a 33% increase. Asia-Pacific revenues consisted of recurring revenues of $9.6 million and $7.1 million, respectively, for the three months ended September 30, 2006 and 2005, consisting primarily of colocation and managed infrastructure services. In addition, Asia-Pacific revenues consisted of non-recurring revenues of $549,000 and $492,000, respectively, for the three months ended September 30, 2006 and 2005. Asia-Pacific non-recurring revenues included $42,000 of contract settlement revenue for the three months ended September 30, 2005. Asia-Pacific revenues are generated from Hong Kong, Singapore, Sydney and Tokyo, with Singapore representing approximately 39% and 44%, respectively, of the regional revenues for the three months ended September 30, 2006 and 2005. Our Asia-Pacific colocation revenues are similar to the revenues that we generate from our U.S. IBX centers; however, our Singapore IBX center has additional managed infrastructure service revenue, such as mail service and managed platform solutions, which we do not currently offer in any other IBX center location. The growth in our Asia-Pacific revenues is primarily the result of an increase in the customer base in this region during the past year, particularly in Hong Kong, Sydney and Tokyo.

Cost of Revenues. Cost of revenues were $49.1 million for the three months ended September 30, 2006 as compared to $41.0 million for the three months ended September 30, 2005, a 20% increase. The largest cost components of our cost of revenues are depreciation, rental payments related to our leased IBX centers, utility costs including electricity and bandwidth, IBX employees salaries and benefits, supplies and equipment and security services. A substantial majority of our cost of revenues is fixed in nature and should not vary significantly from period to period. However, there are certain costs, which are considered more variable in nature, including utilities and supplies that are directly related to growth of services in our existing and new customer base. We expect the cost of our utilities, specifically electricity, will increase in the future on a per-unit or fixed basis in addition to on a customer growth or variable basis. In addition, the cost of electricity is generally higher in the summer months as compared to other times of the year.

U.S. Cost of Revenues. U.S. cost of revenues were $43.5 million for the three months ended September 30, 2006 as compared to $35.9 million for the three months ended September 30, 2005. U.S. cost of revenues for the three months ended September 30, 2006 included (i) $16.8 million of depreciation expense, (ii) $895,000 of accretion expense comprised of $138,000 for our asset retirement obligations and $757,000 for our restructuring charges for certain leasehold interests recorded in 2004 and 2005 as we accrete the related liabilities to the total estimated future cash payments needed, (iii) $563,000 of stock-based compensation as a result of our adoption of SFAS 123(R) in the three months ended March 31, 2006 and (iv) $145,000 of amortization expense associated with the intangible assets acquired with our Ashburn campus. U.S. cost of revenues for the three months ended September 30, 2005 included (i) $14.6 million of depreciation expense and (ii) $351,000 of accretion expense comprised of $135,000 for our asset retirement obligations and $216,000 for our restructuring charges. Our U.S. cost of revenues for the three months ended September 30, 2006 also included $3.3 million of additional operating costs not incurred in the prior year associated with the recently opened IBX centers in the Chicago, Los Angeles and Silicon Valley metro areas (the Chicago and Los Angeles IBX centers opened for business during the three months ended June 30, 2006, and the Silicon Valley IBX center opened for business during the three months ending September 30, 2006). Excluding depreciation, accretion expense, stock-based compensation, amortization expense and the costs associated with operating our new IBX centers, U.S. cost of revenues increased period over period to $21.8 million for the three months ended September 30, 2006 from $20.9 million for the three months ended September 30, 2005, a 4% increase. This increase was primarily due to increases in (i) utility costs of approximately $1.8 million in line with increasing customer installations and revenues attributed to customer growth, (ii) compensation costs of approximately $437,000, including general salary increases and bonuses and (iii) repair and maintenance expenses of approximately $358,000. This increase was partially offset by reductions in rent expenses of approximately $1.9 million in connection with a property we recorded a restructuring charge for in San Jose in the fourth quarter of 2005. We continue to anticipate that our cost of revenues will increase in the foreseeable future to the extent that the occupancy levels in our U.S. IBX centers increase and as newly opened IBX centers in the Chicago, Los Angeles and Silicon Valley metro areas commence operations more fully in the remainder of 2006.

Asia-Pacific Cost of Revenues. Asia-Pacific cost of revenues were $5.6 million for the three months ended September 30, 2006 as compared to $5.1 million for the three months ended September 30, 2005. Asia-Pacific cost of revenues for the three months ended September 30, 2006 included (i) $858,000 of depreciation expense, (ii) $101,000 of stock-based compensation as a result of our adoption of SFAS 123(R) in the three months ended March 31, 2006 and (iii) $65,000 of non-cash rent expense associated with the value attributed to warrants issued in May 2004 to our landlord in connection with a lease amendment for our Hong Kong IBX center. Asia-Pacific cost of revenues for the three months ended September 30, 2005 included (i) $845,000 of depreciation expense and (ii) $65,000 of non-cash rent expense. Excluding depreciation, stock-based compensation and non-cash rent expense, Asia-Pacific cost of revenues increased period over period to $4.6 million for the three months ended September 30, 2006 from $4.2 million for the three months ended September 30, 2005, a 10% increase. This increase was primarily the result of increasing utility and bandwidth costs in line with increasing customer installations and revenues attributed to this customer growth. Our Asia-Pacific cost of revenues is generated in Hong Kong, Singapore, Sydney and Tokyo. There are several managed infrastructure service revenue streams unique to our Singapore IBX center, such as mail service and managed platform solutions, that are more labor intensive than our service offerings in the United States. We anticipate that our Asia-Pacific cost of revenues will experience moderate growth in the foreseeable future.

Sales and Marketing. Sales and marketing expenses increased to $7.5 million for the three months ended September 30, 2006 from $4.8 million for the three months ended September 30, 2005.

U.S. Sales and Marketing Expenses. U.S. sales and marketing expenses increased to $6.5 million for the three months ended September 30, 2006 from $4.1 million for the three months ended September 30, 2005. Included in U.S. sales and marketing expenses for the three months ended September 30, 2006 were $1.5 million of stock-based compensation expense and $15,000 of amortization expense associated with an intangible asset in connection with our Santa Clara IBX center. Included in U.S. sales and marketing expenses for the three months ended September 30, 2005 was $248,000 of stock-based compensation expense and $15,000 of amortization expense. The increase in the stock-based compensation expense period over period is a result of our adoption of SFAS 123(R) in the three months ended March 31, 2006. Excluding stock-based compensation and amortization expense, U.S. sales and marketing expenses increased to $5.0 million for the three months ended September 30, 2006 as compared to $3.8 million for the three months ended September 30, 2005, a 31% increase. Sales and marketing expenses consist primarily of compensation and related costs for sales and marketing personnel, sales commissions, marketing programs, public relations, promotional materials and travel. This increase was primarily due to an approximately $606,000 of higher compensation costs, including increases in sales compensation related to strong new customer bookings throughout 2006 and general salary increases and bonuses for our marketing staff and non-commissioned sales staff, and a general increase in other expenses related to our marketing efforts. Going forward, we expect to see U.S. sales and marketing spending to increase nominally in absolute dollars as we continue to grow our business.

Asia-Pacific Sales and Marketing Expenses. Asia-Pacific sales and marketing expenses increased to $1.0 million for the three months ended September 30, 2006 as compared to $751,000 for the three months ended September 30, 2005. Included in Asia-Pacific sales and marketing expenses for the three months ended September 30, 2006 was $129,000 of stock-based compensation as a result of our adoption of SFAS 123(R) commencing in the three months ended March 31, 2006. Excluding stock-based compensation, Asia-Pacific sales and marketing expenses were $884,000 million for the three months ended September 30, 2006 versus $751,000 for the three months ended September 30, 2005, an 18% increase. This increase was primarily due to an increase in travel expense, and bad debt expense of approximately $70,000 over the prior period as a result of recoveries of bad debt expense recorded during the three months ended September 30, 2005 due to a strong and successful collections effort on aged receivables previously written-off. Our Asia-Pacific sales and marketing expenses consist of the same types of costs that we incur in our U.S. operations, namely compensation and related costs for sales and marketing personnel, sales commissions, marketing programs, public relations, promotional materials and travel. Our Asia-Pacific sales and marketing expenses are generated in Hong Kong, Singapore, Sydney and Tokyo. We expect that our Asia-Pacific sales and marketing expenses will experience some moderate growth in the foreseeable future.

General and Administrative. General and administrative expenses increased to $18.6 million for the three months ended September 30, 2006 from $12.1 million for the three months ended September 30, 2005.

U.S. General and Administrative Expenses. U.S. general and administrative expenses increased to $16.1 million for the three months ended September 30, 2006 as compared to $10.0 million for the three months ended September 30, 2005. Included in U.S. general and administrative expenses for the three months ended September 30, 2006 were $4.0 million of stock-based compensation expense and $780,000 of depreciation expense. Included in U.S. general and administrative expenses for the three months ended September 30, 2005 were $1.1 million of stock-based compensation expense and $416,000 of depreciation expense. The increase in the stock-based compensation expense period over period is a result of our adoption of SFAS 123(R) in the three months ended March 31, 2006. Excluding stock-based compensation expense and depreciation expense, U.S. general and administrative expenses increased to $11.3 million for the three months ended September 30, 2006, as compared to $8.5 million for the same period last year, a 32% increase. This increase was primarily due to (i) approximately $306,000 of higher compensation costs, including general salary increases, bonuses and headcount growth (168 U.S. general and administrative employees as of September 30, 2006 versus 150 as of September 30, 2005), (ii) an increase in professional fees of approximately $1.9 million due to increased legal fees in connection with our legal matters such as the ongoing review of our past stock option grants and practices, accounting fees and other consulting projects in connection with our growth strategies and (iii) an increase in rent and other office expenses of $388,000 in connection with our office expansion in Foster City, California. General and administrative expenses, excluding stock-based compensation and depreciation, consist primarily of salaries and related expenses, accounting, legal and other professional service fees and other general corporate expenses such as our corporate headquarter office lease. Going forward, we expect U.S. general and administrative spending to increase as we continue to scale our operations to support our growth and as we incur ongoing professional fees to complete the stock option review and resolve related legal matters.

Asia-Pacific General and Administrative Expenses. Asia-Pacific general and administrative expenses increased to $2.5 million for the three months ended September 30, 2006 as compared to $2.0 million for the three months ended September 30, 2005. Included in Asia-Pacific general and administrative expenses for the three months ended September 30, 2006 was (i) $583,000 of stock-based compensation as a result of our adoption of SFAS 123(R) in the three months ended March 31, 2006 and (ii) $56,000 of depreciation expense. Included in Asia-Pacific general and administrative expenses for the three months ended September 30, 2005 was $60,000 of depreciation expense. Excluding stock-based compensation and depreciation, Asia-Pacific general and administrative expenses decreased to $1.9 million for the three months ended September 30, 2006, as compared to $2.0 million for the same period last year, a nominal 3% decrease. Our Asia-Pacific general and administrative expenses consist of the same types of costs that we incur in our U.S. operations, namely salaries and related expenses, accounting, legal and other professional service fees and other general corporate expenses. Our Asia-Pacific general and administrative expenses are generated in Hong Kong, Singapore, Sydney and Tokyo. Our Asia-Pacific headquarter office is located in Singapore. Most of the corporate overhead support functions that we have in the U.S., such as finance, legal, marketing and information technology, also reside in Singapore in order to support our Asia-Pacific operations; however, each of our Asia-Pacific locations in Hong Kong, Sydney and Tokyo also have general and administrative staff dedicated to each specific operation. In addition to our Asia-Pacific headquarters office in Singapore, we also have separate office locations in Tokyo and Hong Kong (the Sydney general and administrative staff work out of the Sydney IBX center). We expect that our Asia-Pacific general and administrative expenses will experience some moderate growth in the foreseeable future.

Restructuring Charges. During the three months ended September 30, 2006, we recorded an additional restructuring charge of $1.5 million as a result of revised sublease assumptions on two of our excess space leases in the New York and Los Angeles metro areas as a result of new information becoming available. The original restructuring charge for these two leases was recorded in the fourth quarter of 2004 and totaled $17.7 million. We are contractually committed to these two excess space leases through 2015.

Interest Income. Interest income increased to $1.7 million from $1.1 million for the three months ended September 30, 2006 and 2005, respectively. Interest income increased due to higher average cash, cash equivalent and short-term investment balances held in interest-bearing accounts during these periods, as well as higher yields on those balances due to increased interest rates. The average yield for the three months ended September 30, 2006 was 4.74% versus 3.49% for the three months ended September 30, 2005.

Interest Expense. Interest expense increased to $3.6 million from $1.9 million for the three months ended September 30, 2006 and 2005, respectively. The increase in interest expense was primarily due to increases in interest expense associated with the new financings entered into during 2005: (i) the $9.7 million financing for equipment we purchased in connection with our Chicago IBX acquisition in November 2005, which bears interest at 7.50%; (ii) the $38.1 million financing we recorded in connection with our Los Angeles IBX financing in December 2005, which bears interest at 7.75% and (iii) the $60.0 million mortgage payable we recorded in connection with our Ashburn campus financing in December 2005, which bears interest at 8.00%. This increase was partially offset by the conversion activities during the fiscal year 2005 that resulted in a decrease in interest expense. In November 2005, STT Communications converted the remaining 5% of the outstanding 14% convertible secured notes and unpaid interest totaling $2.2 million into 240,578 shares of our preferred stock, which was immediately converted into 240,578 shares of our common stock. Furthermore, in connection with various construction projects related to our IBX expansion

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efforts during the three months ended September 30, 2006, we capitalized $354,000 of interest expense to construction in progress. We did not capitalize any interest during the three months ended September 30, 2005.

Income Taxes. A full valuation allowance is recorded against our net deferred tax assets as management cannot conclude, based on available objective evidence including recurring historical losses, that it is more likely than not that the net value of our deferred tax assets will be realized. However, for the three months ended September 30, 2006, we recorded $270,000 of income tax expense, primarily representing income taxes related to alternative minimum tax and foreign jurisdictions. For the three months ended September 30, 2005, we recorded an income tax expense of $164,000. We have not incurred any significant income tax expense since inception and we do not expect to incur any significant income tax expense during 2006 and 2007 other than alternative minimum tax.

Nine Months Ended September 30, 2006 and 2005

Revenues. Our revenues for the nine months ended September 30, 2006 and 2005 were split between the following revenue classifications (dollars in thousands):

	Nine months ended September 30,			
	2006	%	2005	%
Recurring revenues	$ 196,759	95%	$ 149,623	94%
Non-recurring revenues:				
Installation and professional services	10,363	5%	8,777	5%
Other	21	0%	859	1%
	10,384	5%	9,636	6%
Total revenues	$ 207,143	100%	$ 159,259	100%

Our revenues for the nine months ended September 30, 2006 and 2005 were geographically comprised of the following (dollars in thousands):

	Nine months ended September 30,			
	2006	%	2005	%
U.S. revenues	$ 178,394	86%	$ 137,927	87%
Asia-Pacific revenues	28,749	14%	21,332	13%
Total revenues	$ 207,143	100%	$ 159,259	100%

We recognized revenues of $207.1 million for the nine months ended September 30, 2006 as compared to revenues of $159.3 million for the nine months ended September 30, 2005, a 30% increase. We analyze our business geographically between the U.S. and Asia-Pacific as further discussed below.

Our business is based on a recurring revenue model comprised of colocation, interconnection and managed infrastructure services. We consider these services recurring as our customers are billed on a fixed and recurring basis each month for the duration of their contract, which is generally one to three years in length. Our recurring revenues are a significant component of our total revenues comprising greater than 90% of our total revenues for the nine months ended September 30, 2006 and 2005. Historically, approximately half of our then existing customers order new services in any given quarter representing greater than half of the new orders received in each quarter.

Our non-recurring revenues are primarily comprised of installation services related to a customer s initial deployment and professional services that we perform. These services are considered to be non-recurring as they are billed typically once and only upon completion of the installation or professional services work performed. These non-recurring revenues are typically billed on the first invoice distributed to the customer. Non-recurring installation fees, although generally paid in a lump sum upon installation, are deferred and recognized ratably over the longer of the term of the related contract or expected customer

relationship. As a percent of total revenues, we expect non-recurring revenues to represent less than 10% of total revenues for the foreseeable future. Other non-recurring revenues are comprised primarily of customer settlements, which represent fees paid to us by customers who wish to terminate their contracts with us prior to their expiration.

In addition to reviewing recurring versus non-recurring revenues, we look at two other primary metrics when we analyze our revenues: 1) customer count and 2) utilization. Our customer count increased to 1,260 as of September 30, 2006 versus 1,093 as of September 30, 2005, an increase of 15%. Our utilization rate represents the percentage of our cabinet space billing versus total cabinet space available. Our utilization rate grew to 54% as of September 30, 2006 from 51% as of September 30, 2005; however, excluding the impact of our recent IBX center openings in the Chicago, Los Angeles and Silicon Valley metro areas, our utilization rate would have been 63% as of September 30, 2006. Although we have substantial capacity for growth, our utilization rates vary from market to market among our IBX centers in the eleven markets across the U.S. and Asia-Pacific. We continue to monitor the available capacity in each of our selected markets. To the extent we have limited capacity available in a given market, it may limit our ability for growth in that market. Once capacity becomes limited, we perform demand studies to determine if future expansion is warranted. In addition, power and cooling requirements for some customers are growing on a per unit basis. As a result, customers are consuming an increasing amount of power per cabinet. Although we generally do not control the amount of draw our customers take from installed circuits, we have negotiated power consumption limitations with certain of our high power demand customers. We could face power limitations in our centers even though we may have additional physical capacity available within a specific IBX center. This could have a negative impact on the available utilization capacity of a given center, which could have a negative impact on our ability to grow revenues, affecting our financial performance, operating results and cash flows. As a result of these power limitations in our existing IBX centers, the maximum utilization rate that we expect to achieve for most IBX centers until we consider an IBX center full or sold-out is approximately 75-80% depending on the building configurations. Therefore, consistent with our recent expansion efforts in the Chicago, Los Angeles, Silicon Valley and Washington, D.C. metro area markets, we will continue to closely manage available space and power capacity in each of our operating markets and expect to continue to make strategic and selective expansions to our global footprint when and where appropriate.

U.S. Revenues. We recognized U.S. revenues of $178.4 million for the nine months ended September 30, 2006 as compared to $137.9 million for the nine months ended September 30, 2005, a 29% increase. U.S. revenues consisted of recurring revenues of $169.8 million and $129.8 million, respectively, for the nine months ended September 30, 2006 and 2005, a 31% increase. U.S. recurring revenues consist primarily of colocation and interconnection services plus a nominal amount of managed infrastructure services and, commencing in the fourth quarter of 2005, in connection with our October 2005 purchase of the Ashburn campus property, a nominal amount of recurring rental income from the other tenants located on this property that we now own, which totaled $1.2 million for the nine months ended September 30, 2006. The period over period growth in recurring revenues was primarily the result of an increase in orders from both our existing customers and new customers acquired during the period as reflected in the growth in our customer count and utilization rate as discussed above, and selective price increases in each of our IBX markets. Total increase in revenues as a result of selective price increases for the nine months ended September 30, 2006 over the same period last year was approximately $1.9 million. In addition, we recorded $2.5 million of revenues from our new IBX centers in the Chicago, Los Angeles and Silicon Valley metro areas. We expect our U.S. recurring revenues, particularly colocation and interconnection services, to continue to remain our most significant source of revenue for the foreseeable future.

In addition, U.S. revenues consisted of non-recurring revenues of $8.6 million and $8.1 million, respectively, for the nine months ended September 30, 2006 and 2005. U.S. non-recurring revenues included $817,000 of contract settlement revenue for the nine months ended September 30, 2005. Non-recurring revenues are primarily related to the recognized portion of deferred installation and professional services. U.S. non-recurring revenues, consisting of the recognized portion of deferred installation and professional services, increased 6% period over period, primarily due to strong existing and new customer growth during the year.

Asia-Pacific Revenues. We recognized Asia-Pacific revenues of $28.7 million for the nine months ended September 30, 2006 as compared to $21.3 million for the nine months ended September 30, 2005, a

35% increase. Asia-Pacific revenues consisted of recurring revenues of $27.0 million and $19.8 million, respectively, for the nine months ended September 30, 2006 and 2005, consisting primarily of colocation and managed infrastructure services. In addition, Asia-Pacific revenues consisted of non-recurring revenues of $1.7 million and $1.5 million, respectively, for the nine months ended September 30, 2006 and 2005. Asia-Pacific non-recurring revenues included $21,000 and $42,000 of contract settlement revenue for the nine months ended September 30, 2006 and 2005, respectively. Asia-Pacific revenues are generated from Hong Kong, Singapore, Sydney and Tokyo, with Singapore representing approximately 40% and 46%, respectively, of the regional revenues for the nine months ended September 30, 2006 and 2005. Our Asia-Pacific colocation revenues are similar to the revenues that we generate from our U.S. IBX centers; however, our Singapore IBX center has additional managed infrastructure service revenue, such as mail service and managed platform solutions, which we do not currently offer in any other IBX center location. The growth in our Asia-Pacific revenues is primarily the result of an increase in the customer base in this region during the past year, particularly in Hong Kong, Sydney and Tokyo.

Cost of Revenues. Cost of revenues were $138.0 million for the nine months ended September 30, 2006 as compared to $116.6 million for the nine months ended September 30, 2005, an 18% increase. The largest cost components of our cost of revenues are depreciation, rental payments related to our leased IBX centers, utility costs including electricity and bandwidth, IBX employees salaries and benefits, supplies and equipment and security services. A substantial majority of our cost of revenues is fixed in nature and should not vary significantly from period to period. However, there are certain costs, which are considered more variable in nature, including utilities and supplies that are directly related to growth of services in our existing and new customer base. We expect the cost of our utilities, specifically electricity, will increase in the future on a per unit or fixed basis in addition to on a customer growth or variable basis. In addition, the cost of electricity is generally higher in the summer months as compared to other times of the year.

U.S. Cost of Revenues. U.S. cost of revenues were $121.5 million for the nine months ended September 30, 2006 as compared to $101.6 million for the nine months ended September 30, 2005. U.S. cost of revenues for the nine months ended September 30, 2006 included (i) $47.7 million of depreciation expense, (ii) $2.8 million of accretion expense comprised of $394,000 for our asset retirement obligations and $2.4 million for our restructuring charges for certain leasehold interests recorded in 2004 and 2005 as we accrete the related liabilities to the total estimated future cash payments needed, (iii) $2.0 million of stock-based compensation as a result of our adoption of SFAS 123(R) in the three months ended March 31, 2006 and (iv) $593,000 of amortization expense associated with the intangible assets acquired with our Ashburn campus. U.S. cost of revenues for the nine months ended September 30, 2005 included (i) $42.2 million of depreciation expense and (ii) $1.0 million of accretion expense comprised of $382,000 for our asset retirement obligations and $661,000 for our restructuring charges. Our U.S. cost of revenues for the nine months ended September 30, 2006 also included $6.8 million of additional operating costs not incurred in the prior year associated with the recently opened IBX centers in the Chicago, Los Angeles and Silicon Valley metro areas (the Chicago and Los Angeles IBX centers opened for business during the three months ended June 30, 2006, and the Silicon Valley IBX center opened for business during the three months ending September 30, 2006). Excluding depreciation, accretion expense, stock-based compensation, amortization expense and the costs associated with operating our new IBX centers, U.S. cost of revenues increased period over period to $61.5 million for the nine months ended September 30, 2006 from $58.3 million for the nine months ended September 30, 2005, a 6% increase. This increase was primarily the result of increases in (i) utility costs of approximately $5.4 million in line with increasing customer installations and revenues attributed to customer growth, (ii) compensation costs of approximately $2.1 million, including general salary increases and bonuses and headcount growth and (iii) repair and maintenance expense of approximately $941,000. This increase was partially offset by a reduction of approximately $5.4 million in rent expense in connection with a property we recorded a restructuring charge for in San Jose in the fourth quarter of 2005. We continue to anticipate that our cost of revenues will increase in the foreseeable future to the extent that the occupancy levels in our U.S. IBX centers increase and as newly opened IBX centers in the Chicago, Los Angeles and Silicon Valley metro areas commence operations more fully in the remainder of 2006.

Asia-Pacific Cost of Revenues. Asia-Pacific cost of revenues were $16.5 million for the nine months ended September 30, 2006 as compared to $15.1 million for the nine months ended September 30, 2005. Asia-Pacific cost of revenues for the nine months ended September 30, 2006 included (i) $2.6 million of depreciation expense, (ii) $355,000 stock-based compensation as a result of our adoption of SFAS 123(R) in the three months ended March 31, 2006 and (iii) $195,000 of non-cash rent expense associated with the value attributed to warrants issued in May 2004 to our landlord in connection with a lease amendment for our Hong Kong IBX center. Asia-Pacific cost of revenues for the nine months ended September 30, 2005 included (i) $2.9 million of depreciation expense and (ii) $195,000 of non-cash rent expense. Excluding depreciation, stock-based compensation and non-cash rent expense, Asia-Pacific cost of revenues increased period over period to $13.4 million for the nine months ended September 30, 2006 from $12.0 million for the nine months ended September 30, 2005, a 12% increase. This increase was primarily the result of increasing utility and bandwidth costs in line with increasing customer installations and revenues attributed to this customer growth. Our Asia-Pacific cost of revenues is generated in Hong Kong, Singapore, Sydney and Tokyo. There are several managed infrastructure service revenue streams unique to our Singapore IBX center, such as mail service and managed platform solutions, that are more labor intensive than our service offerings in the United States. We anticipate that our Asia-Pacific cost of revenues will experience moderate growth in the foreseeable future.

Sales and Marketing. Sales and marketing expenses increased to $23.2 million for the nine months ended September 30, 2006 from $14.8 million for the nine months ended September 30, 2005.

U.S. Sales and Marketing Expenses. U.S. sales and marketing expenses increased to $20.1 million for the nine months ended September 30, 2006 from $12.6 million for the nine months ended September 30, 2005. Included in U.S. sales and marketing expenses for the nine months ended September 30, 2006 were $5.2 million of stock-based compensation expense and $45,000 of amortization expense. Included in U.S. sales and marketing expenses for the nine months ended September 30, 2005 was $1.1 million of stock-based compensation expense and $45,000 of amortization expense associated with an intangible asset in connection with our Santa Clara IBX center. The increase in the stock-based compensation expense period over period is a result of our adoption of SFAS 123(R) in the three months ended March 31, 2006. Excluding stock-based compensation and amortization expense, U.S. sales and marketing expenses increased to $14.8 million for the nine months ended September 30, 2006 as compared to $11.4 million for the nine months ended September 30, 2005, a 30% increase. Sales and marketing expenses consist primarily of compensation and related costs for sales and marketing personnel, sales commissions, marketing programs, public relations, promotional materials and travel. This increase was primarily due to (i) approximately $1.9 million of higher compensation costs, including increases in sales compensation related to strong new customer bookings throughout 2006 and general salary increases and bonuses for our marketing staff and non-commissioned sales staff and (ii) approximately $741,000 of higher travel costs. Going forward, we expect to see U.S. sales and marketing spending to increase nominally in absolute dollars as we continue to grow our business.

Asia-Pacific Sales and Marketing Expenses. Asia-Pacific sales and marketing expenses increased to $3.1 million for the nine months ended September 30, 2006 as compared to $2.2 million for the nine months ended September 30, 2005. Included in Asia-Pacific sales and marketing expenses for the nine months ended September 30, 2006 was $435,000 of stock-based compensation as a result of our adoption of SFAS 123(R) commencing in the three months ended March 31, 2006. Excluding stock-based compensation, Asia-Pacific sales and marketing expenses were $2.7 million for the nine months ended September 30, 2006 versus $2.2 million for the nine months ended September 30, 2005, a 22% increase. This increase was primarily due to an increase in bad debt expense of approximately $274,000 over the same period last year as a result of recoveries of bad debt expense recorded during the nine months ended September 30, 2005 (negative bad debt expense) of approximately $142,000 due to a strong and successful collections effort on aged receivables previously written-off. Our Asia-Pacific sales and marketing expenses consist of the same types of costs that we incur in our U.S. operations, namely compensation and related costs for sales and marketing personnel, sales commissions, marketing programs, public relations, promotional materials and travel. Our Asia-Pacific sales and marketing expenses are generated in Hong Kong, Singapore, Sydney and Tokyo. We expect that our Asia-Pacific sales and marketing expenses will experience some moderate growth in the foreseeable future.

General and Administrative. General and administrative expenses increased to $53.5 million for the nine months ended September 30, 2006 from $33.6 million for the nine months ended September 30, 2005.

U.S. General and Administrative Expenses. U.S. general and administrative expenses increased to $44.9 million for the nine months ended September 30, 2006 as compared to $27.7 million for the nine months ended September 30, 2005. Included in U.S. general and administrative expenses for the nine months ended September 30, 2006 were $13.7 million of stock-based compensation expense and $1.8 million of depreciation expense. Included in U.S. general and administrative expenses for the nine months ended September 30, 2005 were $5.1 million of stock-based compensation expense and $1.2 million of depreciation expense. The increase in the stock-based compensation expense period over period is a result of our adoption of SFAS 123(R) in the three months ended March 31, 2006. Excluding stock-based compensation expense and depreciation expense, U.S. general and administrative expenses increased to $29.4 million for the nine months ended September 30, 2006, as compared to $21.4 million for the same period last year, a 38% increase. This increase was primarily due to (i) approximately $2.5 million of higher compensation costs, including general salary increases, bonuses and headcount growth (168 U.S. general and administrative employees as of September 30, 2006 versus 150 as of September 30, 2005), (ii) an increase in professional fees of approximately $3.8 million due to increased legal fees in connection with our legal matters such as the ongoing review of our past stock option grants and practices, accounting fees and other consulting projects in connection with our growth strategies, (iii) an increase in rent, repair and maintenance expenses of approximately $551,000 in connection with our office expansion in Foster City, California and (iv) an increase in travel expenses of approximately $444,000. General and administrative expenses, excluding stock-based compensation and depreciation, consist primarily of salaries and related expenses, accounting, legal and other professional service fees and other general corporate expenses such as our corporate headquarter office lease. Going forward, we expect U.S. general and administrative spending to increase as we continue to scale our operations to support our growth and as we incur ongoing professional fees to complete the stock option review and resolve related legal matters.

Asia-Pacific General and Administrative Expenses. Asia-Pacific general and administrative expenses increased to $8.6 million for the nine months ended September 30, 2006 as compared to $5.9 million for the nine months ended September 30, 2005. Included in Asia-Pacific general and administrative expenses for the nine months ended September 30, 2006 was (i) $1.8 million of stock-based compensation as a result of our adoption of SFAS 123(R) in the three months ended March 31, 2006 and (ii) $191,000 of depreciation expense. Included in Asia-Pacific general and administrative expenses for the nine months ended September 30, 2005 was $223,000 of depreciation expense. Excluding stock-based compensation and depreciation, Asia-Pacific general and administrative expenses increased to $6.6 million for the nine months ended September 30, 2006, as compared to $5.6 million for the same period last year, a 17% increase. This increase is primarily due to approximately $822,000 of higher compensation costs, including general salary increases and bonuses. Our Asia-Pacific general and administrative expenses consist of the same types of costs that we incur in our U.S. operations, namely salaries and related expenses, accounting, legal and other professional service fees and other general corporate expenses. Our Asia-Pacific general and administrative expenses are generated in Hong Kong, Singapore, Sydney and Tokyo. Our Asia-Pacific headquarters office is located in Singapore. Most of the corporate overhead support functions that we have in the U.S., such as finance, legal, marketing and information technology, also reside in our Singapore office in order to support our Asia-Pacific operations; however, each of our Asia-Pacific locations in Hong Kong, Sydney and Tokyo also have general and administrative staff dedicated to each specific operation. In addition to our Asia-Pacific headquarter office in Singapore, we also have separate office locations in Tokyo and Hong Kong (the Sydney general and administrative staff work out of the Sydney IBX center). We expect that our Asia-Pacific general and administrative expenses will experience some moderate growth in the foreseeable future.

Restructuring Charges. During the nine months ended September 30, 2006, we recorded an additional restructuring charge of $1.5 million as a result of revised sublease assumptions on two of our excess space leases in the New York and Los Angeles metro areas as a result of new information becoming available. The original restructuring charge for these two leases was recorded in the fourth quarter of 2004 and totaled $17.7 million. We are contractually committed to these two excess space leases through 2015.

Interest Income. Interest income increased to $5.1 million from $2.6 for the nine months ended September 30, 2006 and 2005, respectively. Interest income increased due to higher average cash, cash equivalent and short-term investment balances held in interest-bearing accounts during these periods, as well as higher yields on those balances due to increased interest rates. The average yield for the nine months ended September 30, 2006 was 4.47% versus 3.11% for the nine months ended September 30, 2005.

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Interest Expense. Interest expense increased to $11.0 million from $6.3 million for the nine months ended September 30, 2006 and 2005, respectively. The increase in interest expense was primarily due to increases in interest expense associated with the new financings entered into during 2005: (i) the $9.7 million financing for equipment we purchased in connection with our Chicago IBX acquisition in November 2005, which bears interest at 7.50%; (ii) the $38.1 million financing we recorded in connection with our Los Angeles IBX financing in December 2005, which bears interest at 7.75% and (iii) the $60.0 million mortgage payable we recorded in connection with our Ashburn campus financing in December 2005, which bears interest at 8.00%. This increase was partially offset by the conversion activities during the fiscal year 2005 that resulted in a decrease in interest expense. In November 2005, STT Communications converted the remaining 5% of the outstanding 14% convertible secured notes and unpaid interest totaling $2.2 million into 240,578 shares of our preferred stock, which was immediately converted into 240,578 shares of our common stock. Furthermore, in connection with various construction projects related to our IBX expansion efforts during the nine months ended September 30, 2006, we capitalized $1.0 million of interest expense to construction in progress. We did not capitalize any interest during the nine months ended September 30, 2005.

Income Taxes. A full valuation allowance is recorded against our net deferred tax assets as management cannot conclude, based on available objective evidence including recurring historical losses, that it is more likely than not that the net value of our deferred tax assets will be realized. However, for the nine months ended September 30, 2006 and 2005, we recorded $870,000 and $553,000, respectively, of income tax expense, primarily representing income taxes related to alternative minimum tax and foreign jurisdictions. We have not incurred any significant income tax expense since inception and we do not expect to incur any significant income tax expense during 2006 and 2007 other than alternative minimum tax.

Cumulative Effect of a Change in Accounting Principle. As a result of our adoption of SFAS No. 123(R), Share-Based Payment, during the nine months ended September 30, 2006, we recorded a reduction of expense totaling $376,000, which is reflected as a cumulative effect of a change in accounting principle on our statement of operations for this period. This amount reflects the application of an estimated forfeiture rate to partially vested employee equity awards as of January 1, 2006 that we accounted for under APB 25, which was primarily for restricted stock awards to our executive officers that were granted during the three months ended March 31, 2005.

Liquidity and Capital Resources

As of September 30, 2006, our total indebtedness was comprised of (i) non-convertible debt and financing obligations totaling $155.0 million from our Washington D.C. metro area IBX capital lease, San Jose IBX equipment and fiber financing, Chicago IBX equipment financing, Los Angeles IBX financing and Ashburn campus mortgage payable and (ii) convertible debt totaling $86.3 million from our convertible subordinated debentures as outlined below.

We believe we have sufficient cash, coupled with anticipated cash generated from operating activities and anticipated cash from financings expected to close in the fourth quarter of 2006 as described below, to meet our currently identified business objectives for at least the next twelve months. As of September 30, 2006, we had $166.3 million of cash, cash equivalents and short-term and long-term investments. Since the quarter ended September 30, 2003, we have generated positive operating cash flow in each quarter and expect this trend to continue throughout the remainder of 2006 and beyond. In addition, as of September 30, 2006, we had $28.3 million of additional liquidity available to us under the $75.0 million Silicon Valley Bank revolving credit line, which was amended in August 2006, in the event we need additional cash to fund expansion activities, fund working capital requirements or pursue attractive strategic opportunities that may become available in the future. In September 2006, we received loan commitments, subject to customary closing conditions, for a total of $150.0 million to finance our Washington, D.C. metro area IBX expansion project and Chicago metro area IBX expansion project in long-term financing arrangements at anticipated rates of approximately 8%, which we expect to close during the fourth quarter of 2006. While we expect that our cash flow from operations will continue to increase, we expect our cash flow used in investing activities, primarily as a result of our expected purchases of property and equipment to complete these expansion projects, will also increase and we expect them to be greater than our cash flows generated from operating activities. As a result, while we believe we have sufficient cash, coupled with anticipated cash generated from operating activities and anticipated cash from financings expected to close in the fourth quarter of 2006, to meet our currently identified business objectives for at least the next twelve months, we will investigate additional financing opportunities in connection with our current and future expansion plans, in order to continue to meet our cash requirements to fund our other capital expenditures, debt service and corporate operating requirements and maintain our cash and working capital position. However, given our limited operating history, additional potential expansion opportunities that we may decide to pursue and other business risks that may cause our operating results to fluctuate, we may not achieve our desired levels of profitability or cash requirements in the future. For further information, refer to Risk Factors in Item 1A of Part II of this Quarterly Report on Form 10-Q below.

Sources and Uses of Cash

Net cash provided by our operating activities was $49.5 million and $49.0 million for the nine months ended September 30, 2006 and 2005, respectively. This increase was primarily due to improved operating results, excluding the increase in stock-back compensation as a result of our adoption of SFAS 123(R) in 2006; however, these improved operating results were mostly offset by additional restructuring charge payments as a result of our 2005 restructuring charge. While this increased level of restructuring charge payments has had an impact on our ability to grow our cash from operating activities, we expect that we will continue to generate cash from our operating activities throughout the remainder of 2006 and beyond.

Net cash used in our investing activities was $121.7 million and $39.0 million for the nine months ended September 30, 2006 and 2005, respectively. Net cash used in investing activities for the nine months ended September 30, 2006 was primarily the result of the capital expenditures required to bring our recently acquired IBX centers in the Chicago, Los Angeles and Silicon Valley metro areas to Equinix standards, the Washington, D.C. metro area IBX expansion project and Chicago metro area expansion project and to support our growing customer base, as well as the net purchases of our short-term and long-term investments and the purchase of our Chicago IBX property in June 2006 for $9.8 million. Net cash used in investing activities during the nine months ended September 30, 2005 was primarily the result of the net purchases of our short-term and long-term investments, as well as capital expenditures required to bring our recently acquired IBX centers in the Silicon Valley and Washington, D.C. metro areas to Equinix standards and to support our growing customer base. For the remainder of 2006 and beyond, we anticipate that our cash used in investing activities, excluding the purchases, sales and maturities of short-term and long-term investments, will primarily be for our capital expenditures, which we expect to be substantial, as well as additional purchases of real estate that we may undertake in the future.

Net cash provided by financing activities was $37.4 million and $6.7 million for the nine months ended September 30, 2006 and 2005, respectively. Net cash provided by financing activities for the nine months ended September 30, 2006, was primarily due to the $40.0 million borrowing from the $75.0 million Silicon Valley Bank revolving credit line that we borrowed in September 2006 and proceeds from the exercises of employee stock options and purchases from our employee stock purchase plan, partially offset by the repayment of the $30.0 million borrowing from the $50.0 million Silicon Valley Bank revolving credit line that we borrowed in October 2005 and principal payments for our capital lease and other financing obligations and Ashburn campus mortgage payable. Net cash provided by financing activities for the nine months ended September 30, 2005, was primarily the result of proceeds from the exercises of warrants and employee stock options and purchases from our employee stock purchase plans, offset primarily by principal payments for our capital lease and other financing obligations. In September 2006, we received loan commitments, subject to customary closing conditions, for a total of $150.0 million to finance our Washington, D.C. metro area IBX expansion project and Chicago metro area IBX expansion project in long-term financing arrangements at anticipated rates of approximately 8%, which we expect to close during the fourth quarter of 2006.

Debt Obligations Non-Convertible Debt

As of September 30, 2006, our non-convertible debt totaled $155.0 million and was comprised of our (i) Washington D.C. metro area IBX capital lease, (ii) San Jose IBX equipment and fiber financing, (iii) Chicago IBX equipment financing, (iv) Los Angeles IBX financing and (v) Ashburn campus mortgage

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payable. Furthermore, as of September 30, 2006, we had utilized $6.7 million of the credit line through the issuance of letters of credit and $40.0 million borrowing, and, as a result, we had $28.3 million of additional liquidity available to us under the $75.0 million Silicon Valley Bank revolving credit line.

Washington D.C. Metro Area IBX Capital Lease. In April 2004, we entered into a long-term lease for a 95,000 square foot data center in the Washington, D.C. metro area. The center is adjacent to our existing Washington D.C. metro area IBX center. This lease, which includes the leasing of all of the IBX plant and machinery equipment located in the building, is a capital lease. We took possession of this property during the fourth quarter of 2004, and as a result, recorded property and equipment assets, as well as a capital lease obligation, totaling $35.3 million. Payments under this lease will be made monthly through October 2019 at an effective interest rate of 8.50% per annum. As of September 30, 2006, principal of $33.9 million remained outstanding under this capital lease.

San Jose IBX Equipment and Fiber Financing. In December 2004, we entered into a long-term lease for a 103,000 square foot data center in San Jose, and at the same time entered into separate agreements to purchase the equipment located within this new IBX center and to interconnect all three of our Silicon Valley area IBX centers to each other through redundant dark fiber links. Under U.S. generally accepted accounting principles, these three separate agreements are considered to be a single arrangement. Furthermore, while the building component of this transaction is classified as a long-term operating lease, the equipment and fiber portions of the transaction are classified as financed assets. We took possession of this property during the first quarter of 2005, and as a result, recorded property and equipment and prepaid fiber assets, as well as a financing obligation, totaling $18.7 million. Payments under this financing obligation will be made monthly through May 2020 at an effective interest rate of 8.50% per annum. As of September 30, 2006, principal of $14.8 million remained outstanding under this financing obligation.

Chicago IBX Equipment Financing. In July 2005, we entered into a long-term sublease for a 107,000 square foot data center in Chicago, and at the same time entered into a separate agreement to purchase the equipment located within this IBX center. Under U.S. generally accepted accounting principles, these two separate agreements are considered to be a single arrangement. Furthermore, while the building component of this transaction is classified as a long-term operating lease, the equipment portion of the transaction is classified as financed assets. We took possession of this property and title to the equipment assets in November 2005, and as a result, recorded IBX equipment assets, as well as a financing obligation, totaling $9.7 million at that time. Payments under this financing obligation will be made monthly through August 2015 at an effective interest rate of 7.50% per annum. As of September 30, 2006, principal of $8.2 million remained outstanding under this financing obligation.

Los Angeles IBX Financing. In September 2005, we purchased a 107,000 square foot data center in the Los Angeles metro area for $34.7 million, which we paid for in full with cash in September 2005. In October 2005, we entered into a purchase and sale agreement to sell this Los Angeles IBX for $38.7 million and to lease it back from the purchaser pursuant to a long-term lease, which closed in December 2005, and we received net proceeds from the sale of this property of $38.1 million. However, due to our continuing involvement in regards to certain aspects of this property, the sale and leaseback of this property does not qualify as a sale-leaseback under generally accepted accounting principles, but rather is accounted for as a financing of the property. We refer to this portion of the transaction as the Los Angeles IBX financing. Pursuant to the Los Angeles IBX financing, we recorded a financing obligation liability totaling $38.1 million in December 2005. Payments under the Los Angeles IBX financing will be made monthly through December 2025 at an effective interest rate of 7.75% per annum. As of September 30, 2006, principal of $38.1 million remained outstanding under this financing obligation.

Ashburn Campus Mortgage Payable. In December 2005, we completed the financing of our October 2005 purchase of the Ashburn campus property with a $60.0 million mortgage to be amortized over 20 years. Upon receipt of the $60.0 million of cash, which we received in December 2005, we recorded a $60.0 million mortgage payable, which we refer to as the Ashburn campus mortgage payable. Payments under the Ashburn campus mortgage payable will be made monthly through January 2026 at an effective interest rate of 8% per annum. As of September 30, 2006, principal of $59.2 million remained outstanding under this mortgage payable.

$75.0 Million Silicon Valley Bank Revolving Credit Line. In December 2004, we entered into a $25.0 million line of credit arrangement with Silicon Valley Bank that matured in December 2006. In September 2005, we amended the Silicon Valley Bank credit line by entering into a $50.0 million revolving line of credit agreement with Silicon Valley Bank, replacing the previously outstanding $25.0 million line of credit arrangement with the same bank. In August 2006, we amended the Silicon Valley Bank credit line by entering into a $75.0 million revolving line of credit agreement with Silicon Valley Bank, replacing the previously outstanding $50.0 million line of credit arrangement with the same bank, and adding General Electric Capital Corporation (GE) as a lender. We refer to this transaction as the $75.0 million Silicon Valley Bank revolving credit line. The $75.0 million Silicon Valley Bank revolving credit line allows for issuance of letters of credit (in addition to revolving borrowings). The $75.0 million Silicon Valley Bank revolving credit line also has an option for us to increase the amount of the line to $100.0 million at a later date, subject to approval of the lender or lenders electing to participate in such increase. Borrowings under the $75.0 million Silicon Valley Bank revolving credit line will continue to bear interest at variable interest rates, plus the applicable margins which were in effect prior to the amendment, based on either prime rates or LIBOR rates. In October 2005, we elected to borrow $30.0 million from the $50.0 million Silicon Valley Bank revolving credit line, which we refer to as the $30.0 million borrowing and which we paid back in full in January 2006. The $30.0 million borrowing was used to fund a portion of the purchase of the Ashburn IBX property acquisition. In September 2006, we elected to borrow $40.0 million from the $75.0 million Silicon Valley Bank revolving credit line, which we refer to as the $40.0 million borrowing, of which $20.0 million of the $40.0 million borrowing was borrowed at the prime rate and bears interest at 8.75% per annum and the remaining $20.0 million was borrowed at a spread over the one-month LIBOR rate and bears interest at 7.824% per annum. The $40.0 million borrowing was used to fund capital expenditures and construction costs related to the Washington D.C. metro area IBX expansion project and Chicago metro area IBX expansion project. As of September 30, 2006, in addition to the $40.0 million borrowing, we had also utilized $6.7 million under the letters of credit sublimit with the issuance of five letters of credit under the $75.0 million Silicon Valley Bank revolving credit line reducing the amount of borrowings available to us from $75.0 million to $28.3 million. These letters of credit automatically renew in successive one-year periods until the final lease expiration dates. If the landlords for any of these five IBX leases decide to draw down on these letters of credit, we will be required to fund these letters of credit either through cash collateral or borrowings under the $75.0 million Silicon Valley Bank revolving credit line. As of September 30, 2006, the $40.0 million borrowing from $75.0 million Silicon Valley Bank revolving credit line had an effective blended interest rate of 8.29% per annum. The $75.0 million Silicon Valley Bank revolving credit line matures on September 15, 2008 and is secured by substantially all of our domestic personal property assets and certain of our real property leases and contains several financial covenants, which require compliance with maximum leverage and working capital ratios and a minimum EBITDA target, all of which we were in compliance with as of September 30, 2006.

In October 2006, we utilized an additional $7.8 million under the letters of credit sublimit associated with the $75.0 million Silicon Valley Bank revolving credit line in connection with the new lease for the New York metro area IBX expansion project and we also fully repaid the $40.0 million borrowing under the $75.0 million Silicon Valley Bank revolving credit line.

Debt Obligations   Convertible Debt

Convertible Subordinated Debentures. During February 2004, we sold $86.3 million in aggregate principal amount of 2.5% convertible subordinated debentures due 2024 to qualified institutional buyers. The interest on the convertible subordinated debentures is payable semi-annually every February and August, which commenced August 2004, and is payable in cash. Our convertible subordinated debentures are convertible into 2.2 million shares of our common stock.

Holders of the convertible subordinated debentures may require us to purchase all or a portion of their debentures on February 15, 2009, February 15, 2014 and February 15, 2019, in each case at a price equal to 100% of the principal amount of the debentures plus any accrued and unpaid interest. In addition, holders of the convertible subordinated debentures may convert their debentures into shares of our common stock upon certain defined circumstances, including during any calendar quarter if the closing price of our common stock is greater than or equal to 120% of $39.50 per share of our common stock, or approximately $47.40 per share, for twenty consecutive trading days during the period of thirty consecutive trading days ending on the last day of the previous calendar quarter. We may redeem all or a portion of the debentures at any time after February 15, 2009 at a redemption price equal to 100% of the principal amount of the debentures plus any accrued and unpaid interest.

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Debt Maturities, Financings, Leases and Other Contractual Commitments

We lease our IBX centers and certain equipment under non-cancelable lease agreements expiring through 2025. The following represents our debt maturities, financings, leases and other contractual commitments as of September 30, 2006 (in thousands):

	Borrowings under credit line and convertible subordinated debentures	Mortgage payable	Capital lease and other financing obligations	Operating leases covered under accrued restructuring charges	Operating leases (1)	Other contractual commitments (1)	Total
2006 (three months remaining)	$ 40,000	$ 1,505	$ 2,348	$ 3,579	$ 7,843	$ 65,420	$ 120,695
2007		6,022	9,568	13,954	31,275	2,609	63,428
2008		6,022	9,842	13,262	31,140	760	61,026
2009	86,250	6,022	10,122	13,309	31,077		146,780
2010		6,022	10,409	3,357	30,047		49,835
2011 and thereafter		90,838	128,354	18,134	155,976		393,302
	126,250	116,431	170,643	65,595	287,358	68,789	835,066
Less amount representing interest		(57,266)	(82,123)				(139,389)
Plus amount representing residual property value			6,555				6,555
Less amount representing estimated subrental income and expense				(14,759)			(14,759)
Less amount representing accretion				(6,291)			(6,291)
	$ 126,250	$ 59,165	$ 95,075	$ 44,545	$ 287,358	$ 68,789	$ 681,182

(1) Represents off-balance sheet arrangements. Other contractual commitments are described below.

In connection with five of our IBX operating leases, we have entered into five irrevocable letters of credit with Silicon Valley Bank. These letters of credit were provided in lieu of cash deposits under the letters of credit sublimit provision in connection with the $75.0 million Silicon Valley Bank revolving credit line. The letters of credit total $6.7 million, are collateralized by the $75.0 million Silicon Valley Bank revolving credit line and automatically renew in successive one-year periods until the final lease expiration dates. If the landlords for any of these five IBX leases decide to draw down on these letters of credit, we will be required to fund these letters of credit either through cash collateral or borrowings under the Silicon Valley Bank revolving credit line. This contingent commitment is not reflected in the table above. In October 2006, we utilized an additional $7.8 million under the letters of credit sublimit associated with the $75.0 million Silicon Valley Bank revolving credit line in connection with the new lease for the New York metro area IBX expansion project.

Primarily as a result of our recent IBX expansions in the Chicago, Los Angeles, Silicon Valley and Washington D.C. metro areas, as of September 30, 2006, we were contractually committed for $61.2 million of un-accrued capital expenditures, primarily for IBX equipment not yet delivered and labor not yet provided, in connection with the work necessary to open these IBX centers prior to making them available to customers for installation. This amount, which is expected to be paid in 2006 and 2007, is reflected in the table above as an other contractual commitment. In addition, although we are not contractually obligated to do so, we expect to incur additional capital expenditures beyond the $61.2 million contractually committed as of September 30, 2006 in these three markets during the remainder of 2006 and the nine months ended September 30, 2007 of approximately $270.0 million to $280.0 million in order to complete the work needed to bring these new IBXs up to Equinix standards. This non-contractual capital expenditure spending is not reflected in the table above. Lastly, we have other, non-capital purchase commitments in place as of September 30, 2006, such as commitments to purchase power in select locations, primarily in the U.S. and Singapore, and other open purchase orders, which contractually bind us for goods or services to be delivered or provided later in 2006 and 2007. Such other purchase commitments as of September 30, 2006, which total $7.6 million, are also reflected in the table above as an other contractual commitments.

Summary

Our utilization rate represents the percentage of our cabinet space billing versus total cabinet space available. Our utilization rate grew to 54% as of September 30, 2006 from 51% as of September 30, 2005; however, excluding the impact of our recent expansions in the Chicago, Los Angeles and Silicon Valley metro areas, our utilization rate would have been 63% as of September 30, 2006. Although we have substantial capacity for growth, our utilization rates vary from market to market among our IBX centers in the eleven markets across the U.S. and Asia-Pacific. We continue to monitor the available capacity in each of our selected markets. To the extent we have limited capacity available in a given market, it may limit our ability for growth in that market. Once capacity becomes limited, we perform demand studies to determine if future expansion is warranted. In addition, power and cooling requirements for some customers are growing on a per unit basis. As a result, customers are consuming an increasing amount of power per cabinet. Although we generally do not control the amount of draw our customers take from installed circuits, we have negotiated power consumption limitations with certain of our high power demand customers. We could face power limitations in our centers even though we may have additional physical capacity available within a specific IBX center. This could have a negative impact on the available utilization capacity of a given center, which could have a negative impact on our ability to grow revenues, affecting our financial performance, operating results and cash flows. As a result of these power limitations in our existing IBX centers, the maximum utilization rate that we expect to achieve for most IBX centers until we consider an IBX center full or sold-out is approximately 75-80% depending on the building configurations.

Strategically, we will continue to look at attractive opportunities to grow our market share and selectively improve our footprint and service offerings, such as our acquisition of the Sprint property in Santa Clara in December 2003, our 2004 expansions in the Washington, D.C. and Silicon Valley metro area markets and our 2005 expansions in the Chicago, Los Angeles and Silicon Valley metro area markets, our 2006 expansions in the Washington, D.C., Chicago and New York metro area markets, which are expected to open in 2007 (see Recent Developments). However, we will continue to be very selective with any similar opportunity. As was the case with these recent expansions in the Washington, D.C., Chicago, Los Angeles and Silicon Valley metro area markets, our expansion criteria will be dependent on demand from new and existing customers, quality of the design, power capacity, access to networks, capacity availability in current market location, amount of incremental investment required by us in the targeted property, lead-time to break-even and in-place customers. Like our recent expansions, the right combination of these factors may be attractive to us. Dependent on the particular deal, these acquisitions may require upfront cash payments and additional capital expenditures or may be funded through long-term financing arrangements in order to bring these centers up to Equinix standards. Property expansion may be in the form of a purchase of real property, as was the case with our recent Washington, D.C. and Chicago metro area property acquisitions, or a short-term or long-term leasing arrangement.

In addition to our successful strategy of acquiring previously or partially built-out centers, we are currently starting new construction to build out new IBX centers in the Washington, D.C. metro area and, on our recently acquired property in the Chicago metro area and New York metro area. As part of our strategy, we will continue to contemplate the possibility of new construction in selective markets where the inventory for high quality data centers is limited. Decisions to build will consider factors such as customer demand, market pricing and the financial returns associated with the construction. Future purchases or construction may be completed by us or with partners or potential customers to minimize the outlay of cash, which can be significant.

We believe we have sufficient cash, coupled with anticipated cash generated from operating activities and anticipated cash from financings expected to close in the fourth quarter of 2006 as described below, to meet our currently identified business objectives for at least the next twelve months. As of September 30, 2006, we had $166.3 million of cash, cash equivalents and short-term and long-term investments. Since the quarter ended September 30, 2003, we have generated positive operating cash flow in each quarter and expect this trend to continue throughout the remainder of 2006 and beyond. In addition, as of September 30, 2006, we had $28.3 million of additional liquidity available to us under the $75.0 million Silicon Valley Bank revolving credit line, which was amended in August 2006, in the event we need additional cash to fund expansion activities, fund working capital requirements or pursue attractive strategic opportunities that may become available in the future. In September 2006, we received loan commitments, subject to customary closing conditions, for a total of $150.0 million to finance our Washington, D.C. metro area IBX expansion project and Chicago metro area IBX expansion project in long-term financing arrangements at anticipated rates of approximately 8%, which we expect to close during the fourth quarter of 2006. While we expect that our cash flow from operations will continue to increase, we expect our cash flow used in investing activities, primarily as a result of our expected purchases of property and equipment to complete these expansion projects, will also increase and we expect them to be greater than our cash flows generated from operating activities. As a result, while we believe we have sufficient cash, coupled with anticipated cash generated from operating activities and anticipated cash from financings expected to close in the fourth quarter of 2006, to meet our currently identified business objectives for at least the next twelve months, we will investigate additional financing opportunities in connection with our current and future expansion plans, in order to continue to meet our cash requirements to fund our other capital expenditures, debt service and corporate operating requirements and maintain our cash and working capital position. However, given our limited operating history, additional potential expansion opportunities that we may decide to pursue and other business risks that may cause our operating results to fluctuate, we may not achieve our desired levels of profitability or cash requirements in the future.

Recent Accounting Pronouncements

In October 2005, the FASB issued FASB Staff Position No. SFAS 13-1 (FSP SFAS 13-1), which addresses the accounting for rental costs associated with building and ground operating leases that are incurred during a construction period. The FASB decided that such rental costs incurred during a construction period shall be recognized as rental expense. A lessee should cease capitalizing rental costs as of the effective date of FSP SFAS 13-1. The guidance in FSP SFAS 13-1 shall be applied to the first reporting period beginning after December 15, 2005. Early adoption is permitted for financial statements or interim financial statements that have not yet been issued. A lessee shall cease capitalizing rental costs as of the effective date of FSP SFAS 13-1 for operating lease arrangements entered into prior to the effective date of FSP SFAS 13-1. The adoption of FSP SFAS 13-1 has not had a significant impact on our financial position, results of operations or cash flows as our accounting policy for such rental costs has always been to expense such costs.

In November 2005, the FASB issued FASB Staff Position No. SFAS 115-1 and SFAS 124-1 (FSP SFAS 115-1 and 124-1), which addresses the determination as to when an investment is considered impaired, whether that impairment is other than temporary, and the measurement of an impairment loss. FSP SFAS 115-1 and 124-1 also includes accounting considerations subsequent to the recognition of an other-than-temporary impairment and requires certain disclosures about unrealized losses that have not been recognized as other-than-temporary impairments. The guidance in FSP SFAS 115-1 and 124-1 amends FASB Statements No. 115, Accounting for Certain Investments in Debt and Equity Securities, and No. 124, Accounting for Certain Investments Held by Not-for-Profit Organizations, and APB Opinion No. 18, The Equity Method of Accounting for Investments in Common Stock. The guidance in FSP SFAS 115-1 and 124-1 shall be applied to the first reporting period beginning after December 15, 2005. The adoption of FSP SFAS 115-1 and 124-1 has not had a significant impact on our financial position, results of operations and cash flows.

In February 2006, the FASB issued SFAS No. 155, Accounting for Certain Hybrid Instruments, an amendment of SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities and SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities-a replacement of FASB Statement No. 125 (SFAS No. 155). SFAS No. 155 improves the financial reporting of certain hybrid financial instruments by requiring more consistent accounting that eliminates exemptions and provides a means to simplify the accounting for such instruments. Specifically, SFAS No. 155 allows financial instruments that have embedded derivatives to be accounted for as a whole (eliminating the need to bifurcate the derivative from its host) if the holder elects to account for the whole instrument on a fair value basis. SFAS No. 155 also (i) clarifies which interest-only strips and principal-only strips are not subject to the requirements of SFAS No. 133; (ii) establishes a requirement to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation; (iii) clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives and (iv) amends SFAS No. 140 to eliminate the prohibition on a qualifying special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument. SFAS No. 155 is effective for all financial instruments acquired or issued after the beginning of an entity s first fiscal year that begins after September 15, 2006. We are currently in the process of evaluating the impact that the adoption of SFAS No. 155 will have on our financial position, results of operations and cash flows.

In April 2006, the FASB issued FASB Staff Position No. FIN 46(R)-6 (FSP FIN 46(R)-6), which addresses how a reporting enterprise should determine the variability to be considered in applying FASB Interpretation No. 46, Consolidation of Variable Interest Entities , as amended (FIN 46(R)). The variability that is considered in applying FIN 46(R) affects the determination of (a) whether the entity is a variable interest entity, (b) which interests are variable interests in the entity and (c) which party, if any, is the primary beneficiary of the variable interest entity. That variability will affect any calculation of expected losses and expected residual returns, if such a calculation is necessary. FSP FIN 46(R)-6 provides additional guidance to consider for determining variability. FSP FIN 46(R)-6 is effective beginning the first day of the first reporting period beginning after June 15, 2006. The adoption of FSP FIN 46(R)-6 has not had a significant impact on our financial position and results of operations.

In June 2006, the FASB approved EITF Issue No. 06-3, How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That is, Gross versus Net Presentation) (EITF 06-3). EITF 06-3 includes any tax assessed by a governmental authority that is directly imposed on a revenue-producing transaction between a seller and a customer and may include, but is not limited to, sales, use, value added and some excise taxes. EITF 06-3 concludes that the presentation of taxes on either a gross (included in revenue and costs) or a net (excluded from revenue) basis is an accounting policy decision that should be disclosed. In addition, for any such taxes that are reported on a gross basis, an entity should disclose the amounts of those taxes in interim and annual financial statements for each period for which an income statement is presented if those amounts are significant. The provisions of EITF 06-3 should be applied to financial reports for interim and annual reporting periods beginning after December 15, 2006, with earlier adoption permitted. We are currently in the process of evaluating the impact that the adoption of EITF 06-3 will have on our financial position, results of operations and cash flows.

In July 2006, the FASB issued Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48), which clarifies the accounting for uncertainty in income taxes recognized in the financial statements in accordance with FASB Statement No. 109, Accounting for Income Taxes. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. We are currently in the process of evaluating the impact that the adoption of FIN 48 will have on our financial position, results of operations and cash flows.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements (SFAS No. 157). SFAS No. 157 defines fair value, establishes a framework for measuring fair value under GAAP, and expands disclosures about fair value measurements. SFAS No. 155 is effective for fiscal years beginning after December 15, 2007. We are currently in the process of evaluating the impact that the adoption of SFAS No. 157 will have on our financial position, results of operations and cash flows.

In September 2006, the SEC issued Staff Accounting Bulletin No. 108, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements (SAB 108), to address diversity in practice in quantifying financial statement misstatements. SAB 108 requires that we quantify misstatements based on their impact on each of our financial statements and related disclosures. We will adopt the provisions of SAB 108 during the fourth quarter of 2006. We are currently in the process of evaluating the impact that the adoption of SAB 108 will have on our financial position, results of operations and cash flows.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Market Risk

The following discussion about market risk disclosures involves forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements. We may be exposed to market risks related to changes in interest rates and foreign currency exchange rates and fluctuations in the prices of certain commodities, primarily electricity.

In the past, we have employed foreign currency forward exchange contracts for the purpose of hedging certain specifically identified net currency exposures. The use of these financial instruments was intended to mitigate some of the risks associated with fluctuations in currency exchange rates, but does not eliminate such risks. We may decide to employ such contracts again in the future. We do not use financial instruments for trading or speculative purposes.

Interest Rate Risk

Our exposure to market risk resulting from changes in interest rates relates primarily to our investment portfolio. All of our cash equivalents and marketable securities are designated as available-for-sale and are therefore recorded at fair market value on our balance sheet with the unrealized gains or losses reported as a separate component of other comprehensive income or loss. The fair market value of our marketable securities could be adversely impacted due to a rise in interest rates, but we do not believe such impact would be material. Securities with longer maturities are subject to a greater interest rate risk than those with shorter maturities and as of September 30, 2006 our portfolio maturity was relatively short. If current interest rates were to increase or decrease by 10% from their position as of September 30, 2006, the fair market value of our investment portfolio could increase or decrease by approximately $314,000.

An immediate 10% increase or decrease in current interest rates from their position as of September 30, 2006 would furthermore not have a material impact on our debt obligations due to the fixed nature of the majority of our debt obligations. However, the interest expense associated with our $75.0 million revolving credit line, which bears interest at floating rates, plus applicable margins, based on either the prime rate or LIBOR, could be affected. In October 2005, we elected to borrow $30.0 million at a one-month LIBOR interest rate, inclusive of the applicable margin, of 5.72% per annum. Upon the one-month maturity date of the $30.0 million borrowing, we had the opportunity to either repay all or a portion of the $30.0 million borrowing, or convert the $30.0 million borrowing into a new borrowing at either the then applicable one, three or six month LIBOR rate plus an applicable margin or at the prime rate. We elected to continue rolling this borrowing forward in monthly increments at the then applicable one-month LIBOR interest rates, inclusive of the applicable margin, until such time that we decided to repay the $30.0 million borrowing in full in January 2006 at which point the effective interest rate had risen to 6.12%. In September 2006, we elected to borrow $40.0 million from the $75.0 million Silicon Valley Bank revolving credit line, of which $20.0 million of the $40.0 million borrowing was borrowed at the prime rate and bears interest at 8.75% per annum and the remaining $20.0 million was borrowed at a spread over the one-month LIBOR rate and bears interest at 7.824% per annum. As of September 30, 2006, the effective blended interest rate of our $40.0 million borrowing from the $75.0 million Silicon Valley Bank revolving credit line, which was repaid in full in October 2006, was 8.29% per annum. Any borrowings from our $75.0 million Silicon Valley Bank revolving credit line are subject to interest rate risk.

The fair market value of our long-term fixed interest rate debt is subject to interest rate risk. Generally, the fair market value of fixed interest rate debt will increase as interest rates fall and decrease as interest rates rise. These interest rate changes may affect the fair market value of the fixed interest rate debt but do not impact our earnings or cash flows. The fair market value of our convertible subordinated debentures is based on quoted market prices. The estimated fair value of our convertible subordinated debentures as of September 30, 2006 was approximately $131.2 million versus approximately $98.9 million as of December 31, 2005.

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Foreign Currency Risk

The majority of our recognized revenue is denominated in U.S. dollars, generated mostly from customers in the U.S. However, approximately 14% of our revenues and costs are in the Asia-Pacific region, and a large portion of those revenues and costs are denominated in a currency other than the U.S. dollar, primarily the Singapore dollar, Japanese yen and Hong Kong and Australian dollars. As a result, our operating results and cash flows are impacted by currency fluctuations relative to the U.S. dollar. Going forward, we continue to expect that approximately 13-15% of our revenues and costs will continue to be generated and incurred in the Asia-Pacific region in currencies other than the U.S. dollar.

Furthermore, to the extent that our international sales are denominated in U.S. dollars, an increase in the value of the U.S. dollar relative to foreign currencies could make our services less competitive in the international markets. Although we will continue to monitor our exposure to currency fluctuations, and when appropriate, may use financial hedging techniques in the future to minimize the effect of these fluctuations, there can be no assurance that exchange rate fluctuations will not adversely affect our financial results in the future.

Commodity Price Risk

Certain operating costs incurred by us are subject to price fluctuations caused by the volatility of underlying commodity prices. The commodities most likely to have an impact on our results of operations in the event of price changes are electricity and supplies and equipment used in our IBX centers. We are closely monitoring the cost of electricity at all of our locations.

In addition, as we now intend to start building new, greenfield IBX centers, we will be subject to commodity price risk for building materials related to the construction of these IBX centers, such as steel and copper. In addition, the lead-time to procure certain pieces of equipment, such as generators, is substantial. Any delays in procuring the necessary pieces of equipment for the construction of our IBX centers could delay the anticipated openings of these new IBX centers and, as a result, increase the cost of these projects.

We do not employ forward contracts or other financial instruments to hedge commodity price risk.

Item 4. Controls and Procedures

(a) ***Evaluation of Disclosure Controls and Procedures.*** Our Chief Executive Officer and our Chief Financial Officer, after evaluating the effectiveness of our disclosure controls and procedures (as defined in the Securities Exchange Act of 1934 (the Exchange Act) Rules 13a-15(e) or 15d-15(e)) as of the end of the period covered by this quarterly report, have concluded that our disclosure controls and procedures are effective based on their evaluation of these controls and procedures required by paragraph (b) of Exchange Act Rules 13a-15 or 15d-15.

(b) ***Changes in Internal Control over Financial Reporting.*** There were no changes in our internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Exchange Act Rules 13a-15 or 15d-15 that occurred during our last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

On July 30, 2001 and August 8, 2001, putative shareholder class action lawsuits were filed against us, certain of our officers and directors (the Individual Defendants), and several investment banks that were underwriters of our initial public offering. The cases were filed in the United States District Court for the Southern District of New York, purportedly on behalf of investors who purchased our stock between August 10, 2000 and December 6, 2000. In addition, similar lawsuits were filed against approximately 300 other issuers and related parties. The purported class action alleges violations of Sections 11 and 15 of the Securities Act of 1933 and Sections 10(b), Rule 10b-5 and 20(a) of the Securities Exchange Act of 1934 against us and the Individual Defendants. The plaintiffs have since dismissed the Individual Defendants without prejudice. The suits allege that the underwriter defendants agreed to allocate stock in our initial public offering to certain investors in exchange for excessive and undisclosed commissions and agreements by those investors to make additional purchases in the aftermarket at pre-determined prices. The plaintiffs allege that the prospectus for our initial public offering was false and misleading and in violation of the securities laws because it did not disclose these arrangements. The action seeks damages in an unspecified amount. On February 19, 2003, the Court dismissed the Section 10(b) claim against us, but denied the motion to dismiss the Section 11 claim.

In July 2003, a Special Litigation Committee of the Equinix Board of Directors approved a settlement agreement and related agreements which set forth the terms of a settlement between us, the Individual Defendants, the plaintiff class and the vast majority of the other approximately 300 issuer defendants and the individual defendants currently or formerly associated with those companies. Among other provisions, the settlement provides for a release of us and the individual defendants and our agreeing to assign away, not assert, or release certain potential claims we may have against our underwriters. The settlement agreement also provides a guaranteed recovery of $1 billion to plaintiffs for the cases relating to all of the approximately 300 issuers. To the extent that the underwriter defendants settle all of the cases for at least $1 billion, no payment will be required under the issuers settlement agreement. To the extent that the underwriter defendants settle for less than $1 billion, the issuers are required to make up the difference. On April 20, 2006, JPMorgan Chase and the plaintiffs reached a preliminary agreement for a settlement for $425 million. The Court has not yet approved the JPMorgan Chase settlement. However, if it is finally approved, then the maximum amount that the issuers insurers will be potentially liable for is $575 million. It is anticipated that any potential financial obligation of Equinix to plaintiffs pursuant to the settlement, of which such claims are currently expected to be less than $3.4 million, will be covered by existing insurance and we do not expect that the settlement will involve any payment by us. However, if the JPMorgan Chase settlement is finally approved, Equinix s maximum financial obligation to the plaintiffs pursuant to the settlement agreement would be less than $2 million. We have no information as to whether there are any material limitations on the expected recovery by other issuer defendants of any potential financial obligation to plaintiffs from their own insurance carriers. On February 15, 2005, the court granted preliminary approval of the settlement agreement, subject to certain modifications consistent with its opinion. Those modifications have been made. On March 20, 2006, the Underwriter Defendants submitted objections to the settlement to the Court. The Court held a hearing regarding these and other objections to the settlement at a fairness hearing on April 24, 2006, but has not yet issued a ruling. There is no assurance that the court will grant final approval to the settlement. As approval by the Court cannot be assured, we are unable at this time to determine whether the outcome of the litigation would have a material impact on our results of operations, financial condition or cash flows.

On October 13, 2004, the Court certified a Section 11 class in four of the six cases that were the subject of class certification motions and determined that the class period for Section 11 claims is the period between the initial public offering and the date that unregistered shares entered the market. The Court noted that its decision on those cases is intended to provide strong guidance to all parties regarding class certification in the remaining cases. The Underwriter Defendants sought leave to appeal the class certification decision and the Second Circuit has accepted the appeal. Plaintiffs have not yet moved to certify a class in the Equinix case. Until the settlement is finalized and approved by the Court, or in the event such settlement is not approved, we and our officers and directors intend to continue to defend the actions vigorously.

In June 2006, we received an informal inquiry from the Securities and Exchange Commission (SEC) and a grand jury subpoena from the U.S. Attorney from the Northern District of California (U.S. Attorney) requesting documents relating to our stock option grants and practices. Such inquiries are believed to be related to recent widespread investigations into the practices of public companies relating to the timing of option grants. We intend to fully cooperate in all government investigations.

On June 29, 2006 and September 18, 2006, shareholder derivative complaints were filed in the Superior Court of the State of California, County of San Mateo against certain of our current and former officers and directors (the Defendants). The complaints allege that the Defendants breached their fiduciary duties by engaging in allegedly improper stock option grant practices since at least 2000, and by failing to adequately disclose such transactions. The complaints seek unspecified monetary damages,

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corporate governance changes and restitution. On October 13, 2006, a third shareholder derivative complaint related to allegedly improper stock option grant practices was filed in the United States District Court for the Northern District of California against certain of our current and former officers and directors. The complaint seeks unspecified monetary and punitive damages, corporate governance changes, and the imposition of a constructive trust over certain stock options and related proceeds. At the appropriate time, we expect to file motions to dismiss these lawsuits due to the plaintiffs unexcused failure to make a demand on us before filing the actions. In addition to the current derivative claims, we may be subject to additional derivative or other lawsuits that may be presented on an individual or class basis alleging claims based on our stock option granting practices. Similar lawsuits and investigations have been commenced against numerous other companies based on similar allegations.

Responding to, investigating and/or defending against civil litigations and government inquiries regarding our stock option grants and practices will present a substantial cost to us in both cash and the attention of certain management and may have a negative impact on our operations. In addition, in the event of any negative finding or assertion by the SEC, U.S. Attorney, court of law or any third party claim related to our stock option granting practices, we may be liable for damages, fines or other civil or criminal remedies or remedial actions, or be required to restate our prior period financial statements or adjust our current period financial statements. Any such adverse action could have a material adverse effect on our business and current market value.

Item 1A. Risk Factors

In addition to the other information contained in this report, the following risk factors should be considered carefully in evaluating our business and us:

Risks Related to Our Business

We have incurred substantial losses in the past and may continue to incur additional losses in the future.

Although we have generated cash from operations since the quarter ended September 30, 2003, for the years ended December 31, 2005, 2004 and 2003, we incurred net losses of $42.6 million, $68.6 million and $84.2 million, respectively. For the nine months ended September 30, 2006, we incurred additional net losses of $15.5 million. Although we believe we are approaching a position of having our net losses decrease to a breakeven level or even possibly producing some nominal level of net income in the foreseeable future, we are also currently investing heavily in our future growth through the build-out of several additional IBX centers. As a result, we will have additional depreciation and other operating expenses that will negatively impact our ability to achieve and sustain profitability until these new IBX centers generate enough revenue to exceed their operating costs and cover our additional overhead needed to scale our business for this anticipated growth. Although our goal is to achieve profitability, there can be no guarantee that we will become profitable, and we may continue to incur additional losses. Even if we achieve profitability, given the competitive and evolving nature of the industry in which we operate, we may not be able to sustain or increase profitability on a quarterly or annual basis.

We expect our operating results to fluctuate.

We have experienced fluctuations in our results of operations on a quarterly and annual basis. The fluctuations in our operating results may cause the market price of our common stock to decline. We expect to experience significant fluctuations in our operating results in the foreseeable future due to a variety of factors, including:

- financing or other expenses related to the acquisition, purchase or construction of additional IBX centers;
- mandatory expensing of employee stock-based compensation, including restricted shares;
- demand for space, power and services at our IBX centers;
- changes in general economic conditions and specific market conditions in the telecommunications and Internet industries;

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- costs associated with the write-off or exit of unimproved or underutilized property;
- the provision of customer discounts and credits;
- the mix of current and proposed products and services and the gross margins associated with our products and services;
- the timing required for new and future centers to open or become fully utilized;
- competition in the markets in which we operate;
- conditions related to international operations;
- increasing repair and maintenance expenses in connection with aging IBX centers;
- not enough available capacity in our existing IBX centers to book new revenue or delays in opening up new or acquired IBX centers may delay our ability to book new revenue in markets which have otherwise reached capacity;
- the timing and magnitude of other operating expenses, including taxes, capital expenditures and expenses related to the expansion of sales, marketing, operations and acquisitions, if any, of complementary businesses and assets; and
- the cost and availability of adequate public utilities, including power.

Any of the foregoing factors, or other factors discussed elsewhere in this report could have a material adverse effect on our business, results of operations and financial condition. Although we have experienced growth in revenues in recent quarters, this growth rate is not necessarily indicative of future operating results. It is possible that we may never generate net income on a quarterly or annual basis. In addition, a relatively large portion of our expenses is fixed in the short-term, particularly with respect to lease and personnel expenses, depreciation and amortization, and interest expenses. Therefore, our results of operations are particularly sensitive to fluctuations in revenues. As such, comparisons to prior reporting periods should not be relied upon as indications of our future performance. In addition, our operating results in one or more future quarters may fail to meet the expectations of securities analysts or investors. If this occurs, we could experience an immediate and significant decline in the trading price of our stock.

We are exposed to potential risks from the results of any regulatory review of past stock option grants and practices or any litigation relating to such grants and practices.

As further described in Note 11 of our Notes to Condensed Consolidated Financial Statements in Item 1 of this Quarterly Report on Form 10-Q, the Audit Committee of our Board of Directors has completed an internal review and analysis of our stock option practices and related accounting, as well as our adjustment to our current financial statements resulting from such review. However, we have received an informal inquiry from the Securities and Exchange Commission (SEC) and a subpoena from the United States Attorney s Office, Northern District of California (U.S. Attorney) relating to our stock option practices and the Audit Committee s findings are still subject to review by both entities. There can be no assurance that either the SEC or the U.S. Attorney will agree with the Audit Committee s conclusions.

In addition, two shareholder derivative complaints were filed in the Superior Court of the State of California, County of San Mateo against certain of our current and former officers and directors. The complaints allege that the defendants breached their fiduciary duties by engaging in allegedly improper stock option grant practices since at least 2000, and by failing to adequately disclose such transactions. The complaints seek unspecified monetary damages, corporate governance changes and restitution. A third shareholder derivative complaint related to allegedly improper stock option grant practices was filed in the United States District Court for the Northern District of California against certain of our current and former officers and directors. The complaint seeks unspecified monetary and punitive damages, corporate governance changes, and the imposition of a constructive trust over certain stock options and proceeds.

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We cannot predict the outcome of any of the inquiries, investigations, litigation or other proceedings relating to our stock option practices. We, or our current and former officers and directors, could also become the subject of other regulatory investigations or derivative and other lawsuits that may be presented on an individual or class basis alleging claims based on our stock option granting practices.

Responding to, investigating and/or defending against government inquiries and civil litigations regarding our stock option grants and practices will present a substantial cost to us in both cash and the attention of certain management and may have a negative impact on our operations. Our current and former officers and directors could also seek indemnification or advancement or reimbursement of expenses from us, including attorneys fees, with respect to the ongoing proceedings mentioned and any subsequent proceedings. In addition, in the event of any negative finding or assertion by the SEC, U.S. Attorney, court of law or any third party claim related to our stock option granting practices, we may be liable for damages, fines or other civil or criminal remedies or remedial actions, or be required to restate prior period financial statements or adjust current period financial statements.

We are also currently assessing if any negative tax consequences will impact our employees as a result of this matter. When this determination is reached, we may decide to compensate the impacted employees in an amount sufficient to offset any negative tax consequences that they may incur.

Any of these events could adversely affect our business and the price of our common stock.

Our inability to use our tax net operating losses will cause us to pay taxes at an earlier date and in greater amounts, which may harm our operating results.

We believe that our ability to use our pre-2003 tax net operating losses, or NOLs, in any taxable year is subject to limitation under Section 382 of the United States Internal Revenue Code of 1986, as amended, (the Code) as a result of the significant change in the ownership of our stock that resulted from our combination with i-STT Pte. Ltd. and Pihana Pacific, Inc. in 2002, which we call the combination. We expect that a significant portion of our NOLs accrued prior to December 31, 2002 will expire unused as a result of this limitation. In addition to the limitations on NOL carryforward utilization described above, we believe that Section 382 of the Code will also significantly limit our ability to use the depreciation and amortization on our assets, as well as certain losses on the sale of our assets, to the extent that such depreciation, amortization and losses reflect unrealized depreciation that was inherent in such assets as of the date of the combination. These limitations will cause us to pay taxes at an earlier date and in greater amounts than would occur absent such limitations.

We are exposed to potential risks from recent legislation requiring companies to evaluate controls under Section 404 of the Sarbanes-Oxley Act of 2002.

Although we received an unqualified opinion regarding the effectiveness of our internal controls over financial reporting as of December 31, 2004 and December 31, 2005, in the course of our ongoing evaluation of our internal controls over financing reporting, we have identified certain areas which we would like to improve and are in the process of evaluating and designing enhanced processes and controls to address these areas identified during our evaluation, none of which we believe constitutes or will constitute a material change. In addition, the ongoing review of our historical stock option grants and practices and related accounting, discussed elsewhere in this Risk Factors section, may reveal weaknesses in our financial controls and reporting that could require remediation by us. However, we cannot be certain that our efforts will be effective or sufficient for us, or our independent registered public accounting firm, to issue unqualified reports in the future, especially as our business continues to grow and evolve.

It may be difficult to design and implement effective financial controls for combined operations, and differences in existing controls of any acquired businesses may result in weaknesses that require remediation when the financial controls and reporting are combined.

Our ability to manage our operations and growth will require us to improve our operational, financial and management controls, as well as our internal reporting systems and controls. We may not be able to implement improvements to our internal reporting systems and controls in an efficient and timely manner and may discover deficiencies in existing systems and controls.

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If we cannot effectively manage international operations, our revenues may not increase and our business and results of operations would be harmed.

For the years ended December 31, 2005, 2004 and 2003, we recognized 13%, 13% and 15%, respectively, of our revenues outside North America. For both the three and nine months ended September 30, 2006, we recognized 14% of our revenues outside North America. We anticipate that, for the foreseeable future, a significant part of our revenues will be derived from sources outside North America.

To date, the neutrality of our IBX centers and the variety of networks available to our customers has often been a competitive advantage for us. In certain of our acquired IBX centers, in Singapore in particular, the limited number of carriers available reduces that advantage. As a result, we may need to adapt our key revenue-generating services and pricing to be competitive in that market.

We may experience gains and losses resulting from fluctuations in foreign currency exchange rates. To date, the majority of our revenues and costs have been denominated in U.S. dollars; however, the majority of revenues and costs in our international operations have been denominated in Singapore dollars, Japanese yen and Australia and Hong Kong dollars. Although we have in the past and may decide to undertake foreign exchange hedging transactions in the future to reduce foreign currency transaction exposure, we do not currently intend to eliminate all foreign currency transaction exposure. Where our prices are denominated in U.S. dollars, our sales could be adversely affected by declines in foreign currencies relative to the U.S. dollar, thereby making our products more expensive in local currencies. Our international operations are generally subject to a number of additional risks, including:

- the costs of customizing IBX centers for foreign countries;
- protectionist laws and business practices favoring local competition;
- the greater difficulty or delay in accounts receivable collection;
- difficulties in staffing and managing foreign operations;
- political and economic instability;
- our ability to obtain, transfer, or maintain licenses required by governmental entities with respect to the combined business; and
- compliance with evolving governmental regulation with which we have little experience.

We are continuing to invest in our expansion efforts but may not have sufficient customer demand in the future to realize expected returns on these investments.

We are considering the acquisition or lease of additional properties, including construction of new IBX centers beyond those expansion projects already announced. We will be required to commit substantial operational and financial resources to these IBX centers, generally 12-18 months in advance of securing customer contracts, and we may not have sufficient customer demand in those markets to support these centers once they are built. In addition, unanticipated technological changes could affect customer requirements for data centers and we may not have built such requirements into our new IBX centers. Any of these contingencies, if they were to occur, could make it difficult for us to realize expected or reasonable returns on these investments.

We have begun construction of new IBX centers, and may begin construction of additional new IBX centers, which could involve significant risks to our business.

We believe that most of the pre-existing built-out data centers have already been acquired, and that there are few if any viable distressed assets available for us to acquire in our key markets today. In order to sustain our growth in these markets, we must acquire suitable land with or without structures to build our new IBX centers from the ground up (a greenfield build). Greenfield builds are currently underway in the Chicago, Washington D.C. and New York metro areas. A greenfield build involves substantial planning and lead-time, much longer time to completion than we have currently seen in our recent IBX retrofits of existing data centers, and significantly higher costs of construction, equipment, and materials which could have a negative impact on our returns. A greenfield build also requires us to carefully select and rely on the experience of one or several general contractors and associated subcontractors during the construction process. Should a general contractor or significant subcontractor experience financial or other problems during the construction process, we could experience significant delays, increased costs to complete the project, and other negative impacts to our expected returns. Site selection is also a critical factor in our expansion plans, and there may not be suitable properties available in our markets with the necessary combination of high power capacity and fiber connectivity.

While we may prefer to locate new IBX centers adjacent to our existing locations, we may be limited by the inventory and location of suitable properties as well as the need for adequate power and fiber to the site. In the event we decide to build new IBX centers separate from our existing IBX centers, we may provide services to interconnect these two centers. Should these services not provide the necessary reliability to sustain service, this could result in lower interconnection revenue, lower margins, and could have a negative impact on customer retention over time.

If we are not able to generate sufficient operating cash flows or obtain external financing, our ability to fund capital expenditures or fulfill our obligations or execute expansion plans may be limited.

Our capital expenditures, together with ongoing operating expenses and obligations to service our debts, will be a substantial drain on our cash flow and may decrease our cash balances. We regularly assess markets for external financing opportunities, including debt and equity. Additional debt or equity financing may not be available when needed or, if available, may not be available on satisfactory terms. Our inability to obtain needed debt and/or equity financing or to generate sufficient cash from operations may require us to abandon projects or curtail capital expenditures. If we curtail capital expenditures or abandon projects, we could be materially adversely affected.

We may make acquisitions, which pose integration and other risks that could harm our business.

We have recently acquired several new IBX centers, and we may seek to acquire additional IBX centers, real estate for development of new IBX centers, or complementary businesses, products, services or technologies. As a result of these acquisitions, we may be required to incur additional debt and expenditures and issue additional shares of our common stock to pay for the acquired businesses, products, services or technologies, which will dilute our stockholders ownership interest and may delay, or prevent, our profitability. These acquisitions may also expose us to risks such as:

- the possibility that we may not be able to successfully integrate acquired businesses or achieve the level of quality in such businesses to which our customers are accustomed;
- the possibility that additional capital expenditures may be required;
- the possibility that senior management may be required to spend considerable time negotiating agreements and integrating acquired businesses;
- the possible loss or reduction in value of acquired businesses;
- the possibility that our customers may not accept either the existing equipment infrastructure or the look-and-feel of a new or different IBX center;
- the possibility that carriers may find it cost-prohibitive or impractical to bring fiber and networks into a new IBX center;

the possibility of pre-existing undisclosed liabilities regarding the property or IBX center, including but not limited to environmental or asbestos liability, of which our insurance may be insufficient or for which we may be unable to secure insurance coverage; and

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the possibility that the concentration of our IBX centers in the Silicon Valley may increase our exposure to seismic activity and that these centers may be located on or near the fault zones for which we may not have adequate levels of earthquake insurance.

We cannot assure you that the price for any future acquisitions will be similar to prior IBX acquisitions. In fact, we expect acquisition costs, including capital expenditures required to build or render new IBX centers operational, to increase in the future. If our revenue does not keep pace with these potential acquisition and expansion costs, we may not be able to maintain our current or expected margins as we absorb these additional expenses. There is no assurance we would successfully overcome these risks or any other problems encountered with these acquisitions.

The increased use of high power density equipment may limit our ability to fully utilize our IBX centers.

Customers are increasing their use of high-density electrical power equipment, such as blade servers, in our IBX centers which has significantly increased the demand for power on a per cabinet basis. Because most of our centers were built several years ago, the current demand for electrical power may exceed the designed electrical capacity in these centers. As electrical power, not space, is typically the limiting factor in our IBX data centers, our ability to fully utilize our IBX centers may be limited in these centers. The availability of sufficient power may also pose a risk to the successful operation of our new IBX centers. The ability to increase the power capacity of an IBX, should we decide to, is dependent on several factors including, but not limited to, the local utility s ability to provide additional power; the length of time required to provide such power; and/or whether it is feasible to upgrade the electrical infrastructure of an IBX to deliver additional power to customers. Although we are currently designing and building to a much higher power specification, there is a risk that demand will continue to increase and our IBX centers could become obsolete sooner than expected.

Our business could be harmed by prolonged electrical power outages or shortages, increased costs of energy or general lack of availability of electrical resources.

Our IBX centers are susceptible to regional costs of power, electrical power shortages, planned or unplanned power outages such as those that occurred in California during 2001 and in the Northeast in 2003, or from natural disasters such as the tornados in the U.S. East Coast in 2004, and limitations, especially internationally, on availability of adequate power resources. Power outages could harm our customers and our business. We attempt to limit exposure to system downtime by using backup generators and power supplies, however, we may not be able to limit our exposure entirely even with these protections in place, as was the case with power outages we experienced in our Chicago and Washington, D.C. metro area IBX centers in 2005. In addition, the overall power shortage in California has increased the cost of energy, and although contractual price increase clauses may exist, we may not be able to pass these increased costs on to our customers.

In each of our markets, we rely on third parties to provide a sufficient amount of power for current and future customers. At the same time, power and cooling requirements are growing on a per unit basis. As a result, some customers are consuming an increasing amount of power per cabinet. We generally do not control the amount of electric power our customers draw from their installed circuits. This means that we could face power limitations in our centers. This could have a negative impact on the effective available capacity of a given center and limit our ability to grow our business, which could have a negative impact on our financial performance, operating results and cash flows.

We may also have difficulty obtaining sufficient power capacity for potential expansion sites in new or existing markets. We may experience significant delays and substantial increased costs demanded by the utilities to provide the level of electrical service required by our current IBX center designs.

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Increases in property taxes could adversely affect our business, financial condition and results of operations.

Our IBX centers are subject to state and local real property taxes. The state and local real property taxes on our IBX centers may increase as property tax rates change and as the value of the properties are assessed or reassessed by taxing authorities. Many state and local governments are facing budget deficits, which may cause them to increase assessments or taxes. If property taxes increase, our business, financial condition and operating results could be adversely affected.

STT Communications has voting control over a substantial portion of our stock and has influence over matters requiring stockholder consent.

As of September 30, 2006, STT Communications, through its subsidiary, i-STT Investments (Bermuda) Ltd., had voting control over approximately 15% of our outstanding common stock. In addition, STT Communications is not prohibited from buying shares of our stock in public or private transactions. As a result, STT Communications is able to exercise significant control over all matters requiring stockholder approval, including the election of directors and approval of significant corporate transactions, which could prevent or delay a third party from acquiring or merging with us.

We may be forced to take steps, and may be prevented from pursuing certain business opportunities, to ensure compliance with certain tax-related covenants agreed to by us in the combination agreement.

We agreed to a covenant in the combination agreement (which we refer to as the FIRPTA covenant) that we would use all commercially reasonable efforts to ensure that at all times from and after the closing of the combination none of our capital stock issued to STT Communications would constitute United States real property interests within the meaning of Section 897(c) of the Code. Under Section 897(c) of the Code, our capital stock issued to STT Communications would generally constitute United States real property interests at such point in time that the fair market value of the United States real property interests owned by us equals or exceeds 50% of the sum of the aggregate fair market values of (a) our United States real property interests, (b) our interests in real property located outside the U.S., and (c) any other assets held by us which are used or held for use in our trade or business. Currently, the fair market value of our United States real property interests is significantly below the 50% threshold. However, in order to assure compliance with the FIRPTA covenant, we may be limited with respect to the business opportunities we may pursue, particularly if the business opportunities would increase the amounts of United States real property interests owned by us or decrease the amount of other assets owned by us. In addition, we may take proactive steps to avoid our capital stock being deemed United States real property interest, including, but not limited to, (a) a sale-leaseback transaction with respect to some or all of our real property interests, or (b) the formation of a holding company organized under the laws of the Republic of Singapore which would issue shares of its capital stock in exchange for all of our outstanding stock (this reorganization would require the submission of that transaction to our stockholders for their approval and the consummation of that exchange). We will take these actions only if such actions are commercially reasonable for our stockholders and us. We have entered into an agreement with STT Communications and its affiliate pursuant to which we will no longer be bound by the FIRPTA covenant as of September 30, 2009. If we were to breach this covenant, we may be liable for damages to STT Communications.

If regulated materials are discovered at centers leased or owned by us, we may be required to remove or clean-up such materials, the cost of which could be substantial.

We are subject to various environmental and health and safety laws and regulations, including those relating to the generation, storage, handling and disposal of hazardous substances and wastes. Certain of these laws and regulations also impose joint and several liability, without regard to fault, for investigation and cleanup costs on current and former owners and operators of real property and persons who have disposed of or released hazardous substances into the environment. Our operations involve the use of hazardous substances and materials such as petroleum fuel for emergency generators, as well as batteries, cleaning solutions and other materials. In addition, we lease, own or operate real property at which hazardous substances and regulated materials have been used in the past. At some of these locations, hazardous substances or regulated materials are known to be present in soil or groundwater and

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there may be additional unknown hazardous substances or regulated materials present at sites we own, operate or lease. To the extent any hazardous substances or any other substance or material must be cleaned up or removed from such property, we may be responsible under applicable laws, regulations or leases for the removal or cleanup of such substances or materials, the cost of which could be substantial. In addition, noncompliance with existing, or adoption of more stringent, environmental or health and safety laws and regulations or the discovery of previously unknown contamination could require us to incur costs or become the basis of new or increased liabilities that could be material.

Our non-U.S. customers include numerous related parties of STT Communications.

We continue to have contractual and other business relationships and may engage in material transactions with affiliates of STT Communications. Circumstances may arise in which the interests of STT Communications affiliates may conflict with the interests of our other stockholders. In addition, entities affiliated with STT Communications make investments in various companies. They have invested in the past, and may invest in the future, in entities that compete with us. In the context of negotiating commercial arrangements with affiliates, conflicts of interest have arisen in the past and may arise, in this or other contexts, in the future. We cannot assure you that any conflicts of interest will be resolved in our favor.

We depend on a number of third parties to provide Internet connectivity to